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# **Accountability for Performance: The Case of a Tax Administration**

**by**

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## **Declaration**

I certify that this thesis is my own work and does not incorporate any material previously submitted for a degree in any university and that to the best of my knowledge and belief it does not contain any material previously published or written by another person where due reference is not made in the text.

## Abstract

Improving public sector managers' accountability with performance measurement is one of the dominant themes of the New Public Management (NPM) literature. With a case study of HM Customs & Excise (HMCE), this PhD research analyses NPM-inspired accounting changes using evidence from interviews with HMCE personnel, official publications and parliamentary reports. There are four important research findings. First, unlike other service delivery organisations, two sets of competing accountability relationships exist in a tax administration, which are operationalised by two performance measurement regimes. This necessitates adaptation of leading private sector performance measurement models to accommodate the duality. Second, HMCE used accounting as a change vehicle in an attempt to shift emphasis from a traditional, compliance-driven accountability relationship to a customer-focus driven one. Third, the compliance-driven relationship remained the dominant relationship in practice despite implementation of the first round of customer-focused accounting changes. Fourth, a second round of accounting changes, i.e. a *tax gap reduction* approach, attempts to harmonise the two competing performance measurements. This arguably represents a notion of shared accountability of taxpayers and tax administration for 'tax gap' reduction. From an institutional theory perspective, however, adoption of the tax gap approach represents an exercise to (re)gain legitimacy in the eyes of Government. The PhD evidence, therefore, suggests that success of accounting changes is context specific. Moreover, based on a notion of *reciprocity of accountabilities* in the public sector, the PhD research also develops a theoretical framework. This is a significant contribution as existence of multiple accountabilities is recognised in the literature but using accounting changes to shift emphasis from one accountability form to another is not well addressed. In addition to these theoretical contributions, this PhD research is a first field study of PMS of a tax administration, and therefore, also improves our understanding of managerial issues of a neglected, but important, research site.



## **List of Abbreviations**

ACCA	Association of Chartered Certified Accountants
BSC	Balanced Scorecard
CBR	Central Board of Revenue (Pakistan)
CEO	Chief Executive Officer
CIMA	Chartered Institute of Management Accountants
CSR	Comprehensive Spending Review
EFQM	European Foundation for Quality Management
GP	General Practitioner
HMCE	Her Majesty's Customs and Excise
HMRC	Her Majesty's Revenue and Customs
HQs	Head Quarters
HRM	Human Resource Management
IMF	International Monetary Fund
IR	Inland Revenue
LBG	Large Business Group
NAO	National Audit Office
NIS	New Institutional Sociology
NPM	New Public Management
OECD	Organisation for Economic Co-operation and Development
OPA	Outputs Performance and Analyses
PI	Performance Indicator
PMS	Performance Measurement System
PSA	Public Service Agreement
RAB	Resource Accounting & Budgeting
RAF	Reciprocal Accountability Framework
RBS	Regional Business & Services
RDF	Results and Determinants Framework
ROI	Return on Investment
SR	Spending Review
TSC	Treasury Select Committee
UK	United Kingdom
VAT	Value Added Tax
VFM	Value For Money

## **Chapter 1**

### **Introducing the Content and Purpose of the Study**

The ‘New Public Management’ (NPM) strongly advocates greater accountability of the public sector managers so that the public sector performance is improved (Christensen and Laegreid, 1999; Hood, 1995). The PhD study aims to analyse the influence of NPM upon accountability relationships in a tax administration - Her Majesty’s Customs and Excise (HMCE). The research, therefore, is motivated by a desire to improve our understanding of interaction between accountability relationships in the case of a tax administration, in particular, and the use of accounting information for enhancing accountability and organisational performance in the public sector, in general.

The NPM literature claims that public sector managerial practices like quantitative targets and outcomes focused management have shaped the new styles of management in the public sector. The PhD research investigated the extent of such private sector performance measurement practices in the case of a tax administration. The evidence generated by the case study was analysed with the help of insights drawn from institutional and stakeholder theories and the principal-agent model of accountability. Some accounting scholars take the view that the context of an organisation is of primary importance when the change management role of accounting is analysed (Broadbent and Guthrie, 1992). It is worth noting that the period 1997-2003 is important in terms of New Labour’s



agenda of *Modernising Government*. Besides many other policy initiatives, accounting changes ranked high for implementing the reforms agenda. This PhD case study investigates the use of performance measurement for enhancing and modifying accountability relationships in the case of HMCE. It therefore falls within the umbrella term of ‘alternative research’ suggested by Broadbent (1999). As such the PhD research provides an opportunity to research the change management use of accounting and contributes to the academic debate surrounding this issue.

The NPM stresses making ‘customer focus’ the basis of accountability system of all public sector organisations. Why is the context of a tax administration important for an NPM related study? It is because of the dual nature of ‘tax’ – the subject which HMCE administers. In whatever sense<sup>1</sup> the word ‘tax’ is used it often prompts a response of ‘the less, the better’.<sup>2</sup> But the animosity towards taxation and tax collectors is not entirely of recent origin. In fact the legends of *Robin Hood* and *Lady Godiva* are closely related to the public sentiments against taxes<sup>3</sup>. The public sentiment about taxation is best captured by Adam Smith who had himself remained a tax collector: “There is no art which one government sooner learns from another than that of draining money from the pockets of the

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<sup>1</sup> The dictionary meaning of the word ‘tax’ in its generic sense is ‘*strain, heavy demand or burdensome obligation*’ (Oxford, 1998: p 934). In its narrower technical sense the word tax has been defined by OECD as “The term tax is confined to compulsory, unrequited payments to general government” (OECD, 1996: p 3).

<sup>2</sup> ‘*Tax doesn’t need to be taxing*’ is the catchy statement made by the Inland Revenue (now HMRC) in its advertisement campaign. But it does demonstrate how tax is generally viewed by the taxpayers. No wonder tax and tax collectors often attract adverse media coverage. Not only stories hostile to tax collection keep appearing in the print and electronic media but many Hollywood movies have also projected tax collectors as villains. The following website provides a good coverage of such movies and other resources <http://faculty.law.lsu.edu/ccorcos/lawhum/irsfilms.htm>. Interestingly biblical stories also refer to tax collectors as the worst of sinners to whom Jesus offered salvation (Luke 19:9)

<sup>3</sup> For a good coverage on Robin Hood see: [http://en.wikipedia.org/wiki/Robin\\_Hood](http://en.wikipedia.org/wiki/Robin_Hood) and for Lady Godiva see *Lady Godiva: A Literary History of the Legend*, Blackwell, 2002 by Daniel Donoghue

people” (Smith, 1776: p 532). However despite being a cause of numerous mass unrest and political movements<sup>4</sup>, taxation has always remained an indispensable part of statecraft. In fact GDP/tax ratio is considered to be one of the determinants of economic prosperity of a country. This enabling role of taxation is best portrayed by the famous words of Justice Oliver Wendell Holmes inscribed above the entrance of the Internal Revenue Service building in the U.S that “*Taxes are what we pay for a civilized society*” (Simon, 2004: p 2).

From the preceding lines it can be seen that taxation has two competing perspectives. First, those who pay a tax view it as ‘taking away’ therefore they generally aspire to minimise the amount of the tax they pay. This aspiration ranges from evasion (i.e. fraudulent /criminal methods to minimise tax liability) to avoidance (i.e. minimising tax liability by using loopholes in the tax laws). Second, tax revenues help governments finance public spending. In this view tax is ‘giving away’ benefits to those who are not best served by the forces of a pure market economy. Therefore, it can be argued that the two facets of taxation (i.e. ‘taking’ and ‘giving’ away’) have often been a source of dilemma for rulers and those who manage it. The potentially competing perspectives also lead to the difficulty in defining the notions of ‘customers’, ‘customer focus’ and ‘accountability’ which are central to the NPM inspired literature. In the public sector related management accounting literature a few case studies (e.g. Collier, 2001; Broadbent and Laughlin, 1998) have researched the use of accounting as advocated by the NPM for enhancing existing accountability relationships. However there is little research which highlights the complexity in accountability

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<sup>4</sup> Examples are the French Revolution, 1789; the American War of Independence, 1775–1783; the anti-Poll tax riots, 1990 in the U.K.



relationships due to *reciprocity* in such relations. There is no academic literature on accountability and performance measurement systems (PMSs) of tax authorities. This gap in literature becomes more conspicuous when one comes to know that HMCE is one of the oldest public sector organisations (Smith, 1980; Carson, 1972). The PhD research was, therefore, motivated by a desire to investigate the role of accounting in defining or redefining the notion of accountability for performance in a tax administration like HMCE. Informed by experiential knowledge the PhD researcher<sup>5</sup> had the advantage of finding the barriers of technical issues and jargon of a tax administration not insurmountable.

Institutional theorists have argued that the ethos of an organisation is shaped by its historical origins (Stinchcombe, 1965: p154). The PhD research found that the historical origins of the HMCE define the organisation as a law enforcement organisation. It was found that accounting changes were used for reversing the emphasis from the traditional form of accountability to the NPM's 'customer focus' based form of accountability. The analysis of PMSs used by the HMCE during 1997-2003 establishes that the tax administration had a concern for two competing sets of accountability relationships. This finding helped in generalising the relationship of performance measurement to different forms of accountabilities in the case of a tax administration. The general thesis that emerged can be briefly stated in the following lines.

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<sup>5</sup> The PhD author has remained a tax collector in the tax administration of Pakistan

In the case of a tax administration the accountability relationships are of reciprocal nature between the main stakeholders – the tax collectors<sup>6</sup> and the taxpayers, which are operationalised by two competing sets of PMS. One PMS reports performance in terms of the traditional role of holding taxpayers to account for their tax liabilities. The second PMS reports performance in terms of public accountability of the tax collectors to the taxpayers<sup>7</sup>. Applying this generic framework to the HMCE it was found that traditionally the PMS of HMCE had been dominated by the first form of accountability for performance, even though some measures relating to public accountability had also remained included. The NPM inspired accounting changes introduced by the New Labour Government desired to instil customer-focused ethos in the case of all public sector organisations including HMCE. While some studies in other public sector organisations reported use of de-coupling strategies or the effect of full colonisation, this PhD study found in the case of HMCE that the new form of customer-focused accountability through accounting changes had difficulty in coexisting with the traditional ethos/institutions of the organisation. The new form of accountability was thus ultimately redefined and subsumed by the strong organisational ethos. The PhD study, therefore, establishes that off-the-shelf

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<sup>6</sup> In this thesis use of masculine pronouns is only for sake of convenience and signifies neither the gender of the interviewees, nor should it be taken as gender bias of the author, who believes firmly in equality of all irrespective of gender or other differences.

<sup>7</sup> From experiential knowledge the PhD author recalls that in his organisation revenue targets were the only yardstick of organisational and individual performance.. The author can recall how anxiously the berthing of an oil ship at the wharves of Karachi seaport would be awaited as a single ship could help meet the monthly revenue targets. With a faint grin, the author also recollects the statistical tricks that were used to meet the targets. While the departmental notion of performance was unquestionably clear, the taxpayers who interacted with the department had a different set of expectations from the department. Even though verbally there was an emphasis upon good behaviour towards the taxpayers, the formal performance measurement and reporting systems had no provision for the concerns of these external stakeholders. The NPM inspired changes in the UK therefore provided the author with an opportunity to study the shifting of focus from the traditional form of accountability to the new *customer-focused* one.



prescriptions do not work in all situations as the organisational context is not the same across the whole public sector (Boden et al., 1998).

In the budget of 2004, the government in the U.K announced its plan of merging the HMCE with the Inland Revenue (IR) to form a single tax department called HM Revenue and Customs (HMRC). This PhD research does not discuss the mechanics of merger as it can be a topic of a separate research study. However, the evidence of merger does contribute to the findings of the research as same set of reasons are cited for the merger initiative which were earlier cited for implementation of accounting changes. In view of the merger of the HMCE, the PhD research brings one of the oldest public sector organisations into the glare of academic research before it goes into extinction as a distinct organisation. On a more general note the PhD research will be helpful in lifting the barriers for those researchers who might have an interest in researching the managerial issues pertaining to tax authorities.

Researching a big central government organisation is not without challenges and risks. Career bureaucrats often do not fancy being under the spotlight of researchers and analysts. Finding access to the personnel is always a daunting task and the researcher is never privileged with unbridled freedom in asking questions. Even if access is granted to senior managers, they often would tow the official line and say things which are already available in the official publications. The cobweb of research has to be therefore knitted with greater care and subtlety.

Since the PhD research also concerned a big central government department the researcher was naturally also confronted with all such challenges. The difficulty of making the senior managers speak was overcome by making use of oral evidence given by the senior management of the Treasury and HMCE before the parliamentary committees. During these hearings the managers were obliged to answer all types of pleasant and unpleasant questions. Therefore, by collecting textual data from three entirely different sources (in-depth interviews, oral evidence and official documents), effort was made to ensure triangulation so that the evidence is more credible and robust.

Chapters 2-3 of the thesis set the stage for the research by reviewing the relevant literature, explaining the research topic, and the research methodology. Chapter 4 reviews the historical origins of HMCE and explains the law enforcement-based context of the organisation. This analysis is important as the NPM inspired accounting changes of the Government desired to shift the emphasis to the customer-focused management. Chapter 5 proposes a framework for categorising PMSs of tax authorities. The position of the pre-1998 PMS of the HMCE is identified on the figure as “*behaviour*” based where the dominance of traditional form of accountability for revenue collection is quite evident. Chapter 6 reviews the pressures, emanated from the external environment, which support the emphasis shifted to the NPM inspired customer-focused form of accountability. The chapter explains the new performance measurement frameworks introduced by the New Labour government. Chapter 7 examines the effect of new accounting framework as implemented by HMCE and analyses the tensions created by attempts to shift the focus of accountability from the traditional notion



of performance to the new NPM-inspired notion of performance. Chapter 8 builds upon the evidence analysed in the earlier two chapters and develops a generic framework of accountability relationships built around the central notion of reciprocity of accountability between the tax collectors and the taxpayers. Chapter 9 then discusses the tax gap based PSA as the latest approach of the HMCE to reconcile the tensions between the two competing sets of accountabilities identified earlier. In Chapter 10 possible explanations from various perspectives are presented in order to analyse the problems identified in the earlier chapters. Chapter 11 draws upon the analysis of the earlier chapters. It sums up the findings of the research and indicates the possibilities of future research.

## Chapter 2

# **Accountability for Performance in the Public Sector – A Literature Review**

### **Introduction**

In this chapter the literature concerning accountability for performance in the public sector is reviewed. Since the literature is very diverse the aim is to identify the important themes wherein NPM is related to accountability and accounting information. These themes are used in the later chapters for analysing the efforts of operationalising accountability with the help of performance measurement within HMCE. The chapter has three main aims. First, it identifies the important themes of NPM and importance of accountability and performance measurement. Second, it also flags the definitions of focal terms like ‘accountability’, ‘performance’, ‘performance measurement’ and ‘performance management’. Third, it also flags the noticeable gaps in the literature and how this PhD research helps in addressing the gaps. In order to achieve these aims the chapter is organised into four main sections. In section 2.1 a general review of the management accounting literature with regards to the public sector is carried out to establish the need and importance of the PhD research and its positioning within the relevant fields of literature. In section 2.2 important themes of NPM are identified and related to the core issues of accountability and performance measurement. In section 2.3 insights from stakeholder theory and institutional theory are drawn as these are to be used later as analytical tools to examine the

PhD evidence and answer the research questions. In section 2.4 the principal-agent model of accountability is reviewed along with a few examples of theorising accountability and performance measurement in the public sector. Informed by stakeholder theory, institutional theory and the principal-agent model, a simplified model is also proposed for the purpose of this PhD research. Section 2.5 concludes the chapter identifying major themes of literature reviewed and how the PhD thesis will address the gap in the literature.

## **2.1 Management Accounting Research in the Public Sector**

The field of organisational performance has attracted interest of academics and practitioners from a variety of disciplines. Carter et al. (1992: 26) state that it has generated a literature, with roots in the overlapping disciplines of management, accountancy, public administration, social policy and political science, which has further compounded “the conceptual and semantic confusion” surrounding the notion of performance measures. The published literature is therefore very diverse and extends in countless number of directions. However, at a very broad level, one may categorise the literature into three broad themes. First are those writings which analyse reforms that aim at improving overall performance of an organisation. Examples of topics covered under this category are ‘Total Quality Management’ (e.g. McAdam and Saulters, 2000; Chenhall, 1997), ‘EFQM Excellence Model’ (e.g. Udo et al., 2001; Wongrassamee et al., 2003), ‘Just-in-Time’ (e.g. Fullerton and McWatters, 2002; Upton, 1998), and ‘Enterprise Resource Planning’ (e.g. Scapens and Jazayeri, 2003; Granlund and Malmi, 2002).



Second are those writings which pertain mainly to performance appraisal of employees and divisions of an organisation. While the first category analyses organisational level performance, authors falling under the second category (e.g. Mani, 2002; Liden et al., 2001) discuss performance measurement of individuals and associated issues. This category is therefore more 'Human Resource Management' (HRM) focused. Third are those writings which analyse accounting systems for measuring and reporting performance. While many of such writings highlight problematic areas of designing PMS, some (e.g. Kaplan and Norton, 1992) claim that performance measurement is a performance improvement tool as well.

This PhD research analyses the accountability relationships operationalised by performance measurement in HMCE. Therefore while the study is not entirely inattentive to the literature of first two categories, it draws mostly on the literature of the third category.

Survey data suggests that between 40 and 60 per cent of companies significantly changed their PMS between 1995 and 2000 (Frigo and Krumwiede, 1999). Performance measurement is therefore not only of interest to practitioners but has attracted the attention of academics as well. However, a review of the published literature in the mainstream academic accounting journals establishes two important facts. First, despite the fact that there is a growing interest in the management accounting issues of the public sector, the area still lags behind considerably when compared with the research in the private sector. For instance,



Helden (2002) reviews the number of papers published in three accounting journals the *Financial Accountability and Management* (FAM), the *British Accounting Review* (BAR), and the *European Accounting Review* (EAR), and reports the results in the form of the Table 2.1. It can be seen that the research on governmental accounting issues is only 12% of the total papers published in these journals for the period 1999-2001.

Journal	Total No of papers	Papers on governmental management accounting research	Papers on governmental management accounting research as % of total papers
FAM	68	17	25%
BAR	68	9	13%
EAR	112	4	4%
Total	248	30	12%

Table 2.1: Percentage of Papers on Governmental Management Accounting Research in Three Accounting Journals for 1999-2001 (Helden, 2002: p 5)

Second, the research itself is dominated by the case studies of public sector organisations addressing the impact of NPM in the public sector. Pollit (2002) provides a four-tiered classification of NPM-related literature. First, *discursive*, where he research focuses upon the discourse of the NPM implementers. In this stage the research investigates what the authors of official publications say about the purpose of NPM reforms. Second, *decisions*, where the research focuses upon the range of decisions made by the reformers. Third, *implementation*, where the researchers focus upon how the decisions are implemented by the reformers. And finally, *results*, where the researchers investigate the results by comparing them with the claimed benefits of NPM reforms. The author observes that NPM related research has mainly focused upon first two stages, and partly the third stage. However there is little research on the fourth type, i.e. *results*. Helden

(2002) also argues that there is still a need for large scale research on NPM agenda as the existing research is limited in its scope.

Broadbent and Guthrie (1992) carried out a survey of the published literature focusing upon what they call ‘alternative research’. The traditional literature, according to the authors, assumes accounting to be a powerful force of change. The *alternative research* on the other hand comprises two main groups. The first group, like the traditional literature, assumes a change management role of accounting; however, it also recognises the context of an organisation as very important. The second group is more sceptical about a universal change management role of accounting and instead believes that the context of an organisation is of primary importance in success of any organisational change (including accounting changes).

Highlighting the relative paucity of critical research in the said area, the authors suggested the need for international comparisons; work in different sites to those already studied; and studies of different technologies. The authors also called for more questioning of the achievements (or otherwise) of the accounting changes in the public sector. Reviewing the response, Broadbent (1999) concludes that while some progress in the *alternative research* has been witnessed there is still scope for further expansion.

This PhD researcher also carried out an empirical survey of the papers published in four categories of literature, listed in Table 2.2 below. It was found that performance measurement has received wider coverage in the journals falling



under the categories of ‘Operational Management’ and ‘Public Sector’ as compared to the ‘Accounting’ based journals. Surprisingly, the ‘General Management’ based journals have offered the least coverage to the topic as an academic/research issue.

Twenty five journals falling under the category of accounting were included in the analysis (for details see Annex 2.1). Interestingly, public sector related papers are 12.5% of all the papers (i.e. 14 / 112) discussing performance measurement in these journals.

No	Category	Total Journals	Private	public	Total
1	Operations/Production	10	153	13	166
2	Public Administration	19	1	141	142
3	Accounting	25	98	14	112
4	General Management	19	50	9	59
	Total	73	302	177	479

Table 2.2: Summary of coverage of performance measurement as a research topic for period 1980-2002

From the preceding reviews, it emerges that public sector related accounting research is still a minority topic in the mainstream accounting journals. If the focus is turned towards tax authorities there is not a single paper which addresses the management accounting issues of tax authorities in the period reviewed. Tomkins et al. (2001) and Lamb and Lymer (1999) also point out this neglect of an important research site.

The PhD research, therefore, aims to address the calls made by writers like Hopwood (1987; 1983) for case studies that carry out in-depth analysis of the process of accounting changes, by writers like Broadbent and Guthrie (1992) and

Broadbent (1999) for case studies in new sites of alternative research, and by writers like Tomkins et al. (2001) for tax management specific research.

## **2.2 The NPM Debate**

The literature on public sector management in the 1990s has largely centred on the notion of NPM. Some authors (e.g. Martin, 1998, Aucoin, 1995; Hood, 1995, 1991; Zifcak, 1994) sketched the main features of NPM to distinguish it from the traditional form of public administration. These writers refer to various categories of reforms that have been initiated since the 1980s as a “paradigm shift” from the Weberian model of bureaucracy<sup>8</sup> to NPM or the “new managerialism”. NPM has been succinctly defined as “a *loose collection* of ideas, derived primarily from the *private sector*, and *travelling* between countries, generated and certified by *international organisations* like OECD, IMF, and the World Bank” (Christensen and Laegreid, 1999; emphasis added). Power (1997: 43) identifies the desire of the NPM movement as “to replace the presumed inefficiency of hierarchical bureaucracy with the presumed efficiency of markets”.

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<sup>8</sup> Max Weber (1864-1920), an eminent German sociologist and political scientist, is credited with popularising the notion of *bureaucracy*. His seminal work *The Theory of Social and Economic Organisation* (tr. Henderson and Parsons, New York, 1947) outlines how bureaucratic organisations work. According to Weber, the attributes of modern bureaucracy include its impersonality, concentration of the means of administration, a leveling effect on social and economic differences and implementation of a system of authority that is practically indestructible. For further details see *From Max Weber: Essays in Sociology*, trans. and ed. by H. H. Gerth and C. Wright Mills, New York: Oxford University Press, 1946



Put briefly, NPM is about transforming the traditional public administration with the help of specific reform tools. Christensen and Laegreid (1999) cite specific examples of change attempts under NPM reforms as:

- adoption of performance indicators,
- quality system management,
- contracts systems, and
- deregulation.

Hughes, (1998: 4) refers to the various terms used to denote the same phenomenon:

“Though the various terms – new public management, managerialism, entrepreneurial government – may vary, they point to the same phenomenon. This is the replacement of traditional bureaucracy by a new model based on markets. Improving public management, reducing budgets, privatisation of public enterprise seem universal . . .”

Araujo (2001: 918) summarises the distinguishing features between the ‘old’ and ‘new’ management styles in the form of the following table:

Elements	Traditional Administration	NPM
Government organisation	Services provided on a uniform basis operating as single aggregated unit	Break up of traditional structures into quasi-autonomous units
Control of public organisations	Control from the headquarters through the hierarchy of unbroken supervision and checks and balances	Hands-on professional management with clear statement of goals and performance measurement
Control of output measures	Control on inputs and procedures	Stress results and output control rather than procedures
Management practices	Standard established procedures throughout the service	Using private sector management style
Discipline in resources use	Due process and political entitlements	Check resources demands and ‘do more with less’

Table 2.3: Comparison of NPM with traditional bureaucracy (Source: Araujo, 2001 from Hood, 1991).

The NPM and its influence upon individual public sector departments can therefore be studied under various headings. For example, Christensen and Yoshimi (2001) use NPM as a framework for their analysis of performance reporting regimes of Australia and Japan. Using Hood's (1995) articulation of NPM as a set of seven doctrines, the authors observe that the sixth doctrine of using performance measurement as a managerial tool is of central importance to NPM framework. The authors claim that primacy of accounting in NPM has received attention in literature leading to improved terminology resulting in the phrase 'new public financial management' (NPFM) which is defined as:

"development of a performance measurement approach, including techniques such as financial and non-financial performance indicators, league tables, citizen's charters and program evaluations" (Olson et al. 1998, p 18).

From a review of NPM related literature four important interrelated broad themes can be identified. First, it views the existing public management (traditionally called 'public administration') as inefficient and believes that it can be improved by adopting private sector styled managerial practices. For instance, Kaboolian (1998: 64) argues that the main force behind the NPM movement is "to maximize productive and allocative efficiencies that are hampered by 'bureaupathology' that is, public agencies unresponsive to the demands of citizens, led by bureaucrats with the power and incentives to expand their administrative empires and 'policy spaces'". Therefore it can be contended that the advocates of NPM are concerned mainly with reinventing government by effectively translating private sector managerial ideas about quality into the context of public administration.



“One might put the NPM ideal very simply as a desire to replace the presumed inefficiency of hierarchical bureaucracy with the presumed efficiency of markets” (Power, 1997: p 43).

The central feature of NPM can therefore be termed as “lessening or removing differences between the public and the private sector” with the underlying assumption that good managerial practices are applicable to all types of organisations with no distinction of public or private (Hood, 1995; Dunleavy and Hood, 1994)

Second, unlike traditional public administration, performance is not defined in terms of following the rules but instead is gauged on the basis of end results or outcomes. Thus, there is a clear shift in the definition of *performance*. It is not sufficient to be economical in usage of resources in order to be a good performer. The preoccupation with economy makes way to the 3Es (Economy, Efficiency and Effectiveness) which is the most prevalent performance measurement model in the context of the public sector. In this model *economy* refers to minimum utilization of inputs for given outputs, *efficiency* refers to maximum outputs for given inputs, and *effectiveness* refers to achieving success in terms of desired outcomes with the given inputs. *Value for Money* means improvement in all these measures of success (Otley, 2001: p 251).<sup>9</sup> In this approach performance can be termed good if for given monetary resources better results or outcomes are achieved (Lapsley, 1996). In the literature this notion of performance has been explained collectively with the next theme.

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<sup>9</sup> This will be further discussed in Chapters 5 & 7



Third, there is an emphasis on the need for greater accountability of the managers. More importantly, accountability which is defined in ‘public administration’ in terms of economy or limiting corruption, waste and incompetence stands redefined under NPM. Dunleavy and Hood (1994) present this shift in the following figure:

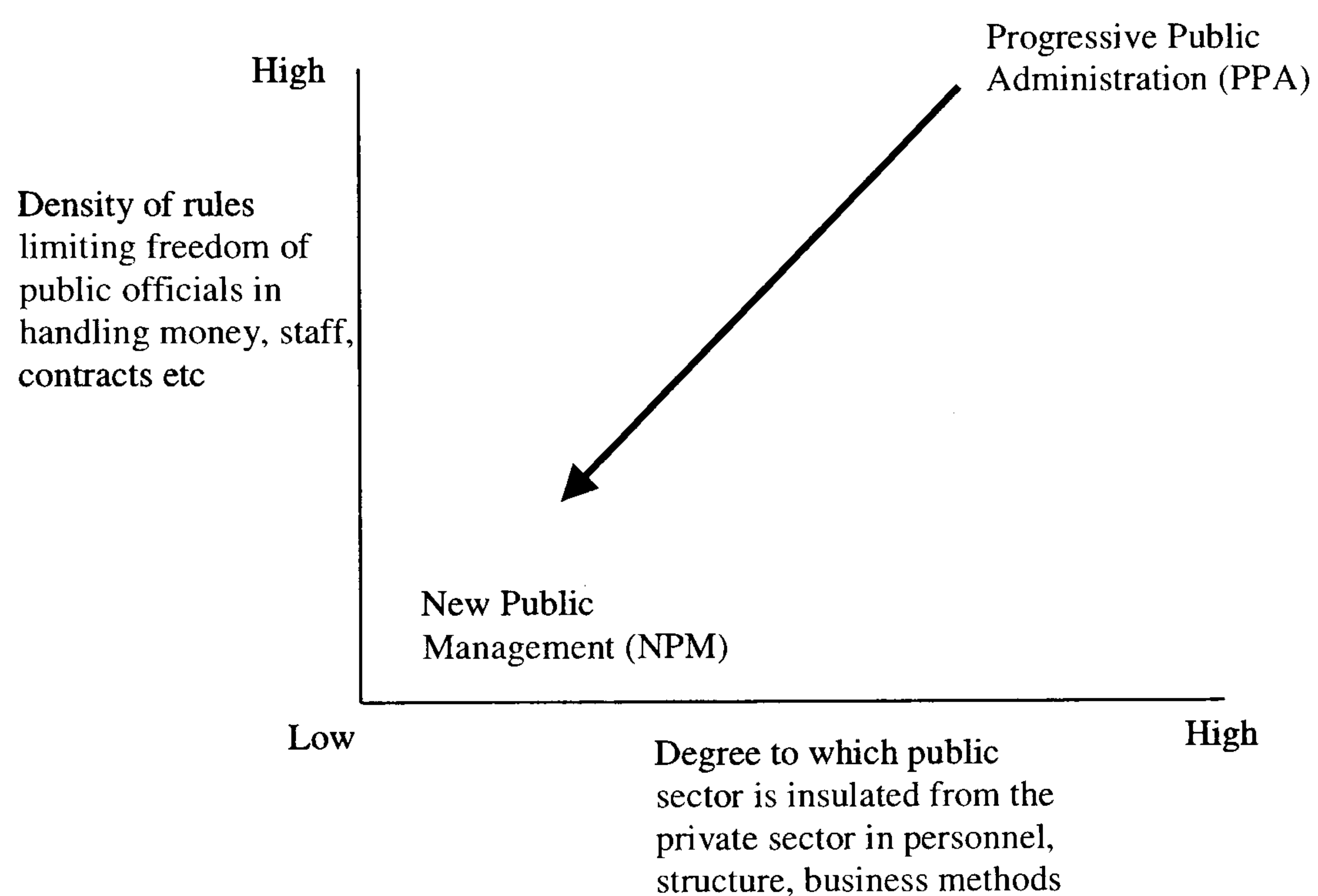


Figure 2.1: From traditional or progressive public administration to new public management (Dunleavy and Hood, 1994: p 10)

Dunleavy and Hood (1994) describe the shift from old public administration to NPM as going ‘down-group’ and going ‘down-grid’. Going ‘down-group’ means making the public sector less distinctive as a unit from the private sector (in personnel, reward structure, methods of doing business). Going ‘down-grid’ means reducing the extent to which discretionary power (particularly over staff, contracts and money) is limited by uniform and general rules of procedure. The main accountability and control tool under the traditional form of public

administration is compliance to *rules and regulations*, such as ensuring that spending is within approved levels and for authorized purposes. Under NPM the emphasis from process accountability gets shifted towards a greater element of accountability for results/outcomes (Hood, 1995).

Fourth, the results-based performance should be monitored with the help of performance measurement. Hood (1995 : 94) identifies ‘more emphasis on visible hands-on top management’; ‘explicit formal measurable standards’; measures of performance and success’ and ‘greater emphasis on output controls’ as the major elements of NPM. The NPM, therefore, was based on the notion that the activities of public servants need to be more closely appraised (in terms of costs) and evaluated by accounting techniques (Hood, 1995: 94; Power and Laughlin, 1992:133). Thus, not only organisational-level performance is assessed with performance targets but it also is generally seen as advocating that governmental organisations be split into business units and assigned performance targets for which managers are held accountable (Gendron et al., 2001).

These elements of NPM and their interrelationship have also been identified by Cunningham and Harris (2001) who observe that the underlying belief of NPM is that *accountability for results* acts as a *control* that leads to *greater effectiveness* in governmental sub-unit *performance*. The causal linkages between accountability, performance measurement, control and effectiveness are plotted by the authors in the following figure:

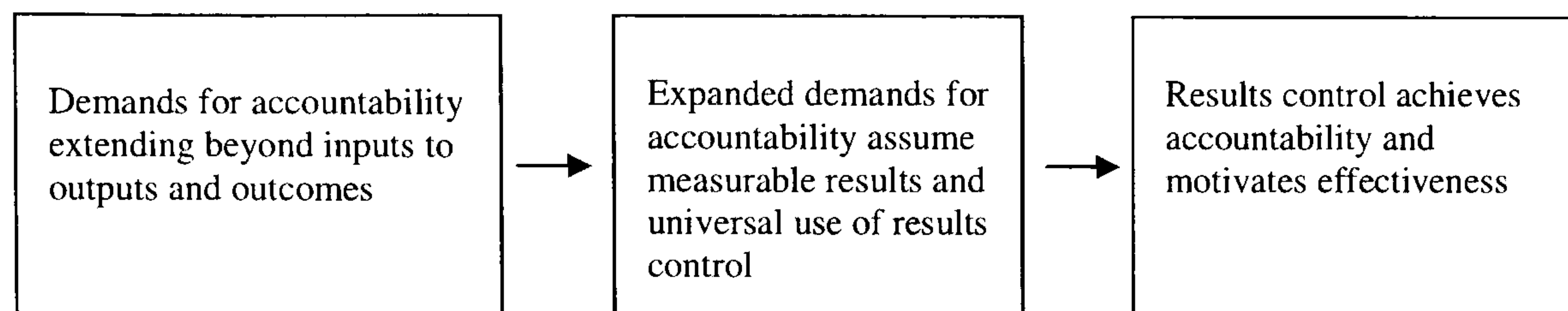


Fig 2.2: Accountability in the new public management (Cunningham and Harris, 2001: p 146)

Thus, briefly, the underlying doctrine of NPM can be seen as improvement of public sector organisations with the help of private sector managerial practices with a firm belief in the power of accounting as a change management tool. It can, therefore, be argued that accountability through accounting tools such as performance measurement emerges as one of the most dominant themes from the NPM literature. In the next sections the interrelationships of NPM, accountability, and performance measurement are examined.

It is claimed by some authors (e.g. Christensen and Yoshimi, 2001) that the NPM movement was given impetus by the influential book *Reinventing Government* of Osborne and Gaebler (1992). In the book the authors stressed the need for a new entrepreneurial global paradigm for public sector management. Greer (1994: 29) contends that “Management consultants also played an important role in packaging, selling, and implementing the NPM reforms”. Some authors on NPM contend that the term “new” does not imply that the concepts of NPM first appeared in the 1980s, as NPM is to a large extent based on a “repackaged version of ideas” that go back at least to the ‘Programming, Planning, and Budgeting System’ (PPBS) movement and thus its development has to be



understood in relation to the “old” public management of the 1960s (Martin, 1998; Hood, 1995).

### **2.2.1 NPM and Accountability for Performance**

From the writings on NPM it emerges that the NPM desires to improve the public sector’s performance by enhancing accountability of the managers for their usage of the resources financed by taxpayers’ money. Thus, ‘accountability’ and ‘performance’ can be identified as the central notions of NPM. It is, therefore, important to investigate their meaning in the literature.

Kane (1996: 125) defines performance in terms of results/outcomes as:

“Performance is the record of outcomes achieved in carrying out a specified job aspect during a specified period”

Brumbach (1988), however, believes that mere *results* can not define performance as *behaviour* is the other important dimension of performance. The author cites the example of a car salesperson that can be rude or courteous while selling a car. The author argues that behaviour emanates from the performer and transforms performance from abstraction to action.<sup>10</sup> He uses a two dimensional typology of *success* and *failure* to view the notion of performance. Performance can be a ‘**positive success**’ if both *results* and *behaviour* were positive. It will be a ‘**negative failure**’ if both *behaviour* and *results* are negative. Performance can be a ‘**negative success**’ if *results* are positive but *behaviour* was negative.

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<sup>10</sup> The author claims that behaviour is not only an instrument for results but is an outcome in its own right as well. According to the author behaviour is the product of mental and physical effort applied to tasks and must be judged separately from immediate results.

Similarly performance can be a ‘**positive failure**’ if *results* are negative but the *behaviour* was positive.

		Results	
		Achieved	Did not Achieve
Behaviour	Positive	Positive Success	Positive Failure
	Negative	Negative Success	Negative Failure

Fig 2.3: The double meanings of ‘Success’ and ‘Failure’ (Brumbach, 1988: p 388)

In contrast with the emphasis on individual performance in the human resource management literature, the discipline of accounting has traditionally remained more interested in organisational-level performance such as profit, return on investment (ROI), and profit margin (Johnson and Kaplan, 1987). Otley (1999) suggests that an organisation that is performing well is one that is successfully attaining its objectives, in other words, one that is effectively implementing an appropriate strategy. In the 1990s many authors (e.g. Kaplan and Norton, 1992; Fitzgerald et al., 1991) advocated multidimensional notions of performance in terms of final results and determinants, or drivers of those results.



**Accountability**<sup>11</sup> is a complex and ‘chameleon-like’ term which is now commonplace in both management accounting and public administration literature (Mulgan, 2000; Sinclair, 1995; Day and Klein, 1987). Mulgan (2000) explores the conceptual meaning of the term *accountability* by analysing extended usages of the term and concludes that while extensions in the meaning of accountability as a concept are understandable, there is a need for preserving **the core sense** of the term which refers to *the external calling of account for one’s actions*<sup>12</sup>. However, before the question of accountability in the public sector is analysed any further it is pertinent to ask why is there a great emphasis upon the notion of accountability under NPM.

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<sup>11</sup> The social psychologists (e.g. Garfinkle, 1967; Mead, 1934) look at *accountability* in the context of identity of the *self* as they try to answer the question: *how do we understand, interpret and explain others and ourselves, and thereby manage to interact with each other in everyday life?* It is argued that all members of a particular social group take for granted that every other member must at the outset ‘know’ the settings in which he is to operate if his practices are to serve as measures to bring particular located features of these settings to recognizable account. Therefore, the accountability of actions is a pervasive matter, and actions are accounted for routinely (Garfinkle, 1967).

<sup>12</sup> Mulgan (2001) argues that over the years the term accountability has increasingly been extended beyond the central concerns emanating from the core meaning. A review of such extended usages is made by the author. He starts by comparing ‘Accountability’ and ‘Responsibility’ and concludes that though sometimes the term responsibility is used interchangeably with accountability, now it is increasingly confined to its more accustomed ethical territory of personal liability, freedom of action and discretion. Then relying mainly upon Day and Klein (1987), the *internal accountability* concept in terms of professional and personal accountability is analysed. It is concluded that the notion of internalised accountability may sometimes be seized on as a last resort by those who feel they ought to be accountable to someone but cannot identify to whom. Another extended usage of accountability is identified as a *mechanism of imposing control* over public organisation. It is also argued that in extended meaning it is sometimes identified with control itself. Yet another extended meaning of *accountability* is identified as *Responsiveness* to the wishes of general public. Here the principle of deliberative democracy has influenced this extended meaning of accountability as a dialogue between the public servants and the public.

Willmott (1996) distinguishes between ‘*universal*’ and ‘*historical forms*’ of accountability where the former applies as an integral part of human nature while the latter is defined by historical and cultural frameworks. Roberts (1991: 365) distinguishes between ‘individualizing’ and ‘socializing’ forms of accountability. He argues that formal hierarchical accountability, in which accounting information plays a central role, is exclusively preoccupied with the strategic or instrumental consequences of action, and thus results in separating broader ethical concerns from the strategic ones. The author makes a case for bringing back instrumental and moral accounting into a relation which the author believes is possible through the mechanism of dialogue.



Two factors can be cited as an explanation. First, many writers on the modern state contend that the emergence of modern state built on the 'contract device' has resulted in erosion of traditional form of ministerial accountability (e.g. Normanton, 1966: p 12; Smith, 1971: p 3-69). Therefore, calls for greater accountability under NPM essentially aim to bring back accountability to the public sector management. Second, the advocates of NPM believe that the private sector managers work under accountability pressures of shareholders and the market. Consequently, the problem of perceived lack of effective accountability in the public sector can be resolved by redefining service delivery in the public sector around notions of customer focus, outcomes and quality improvement. Therefore, the advocates of NPM believe that importing private sector practices in the public sector enhances accountability of the managers.

Rhodes (1997: 5) believes that the recent developments have restrained the traditional mechanisms of democratic accountability. He argues that while the state had been 'hollowed out', *managerial accountability* has been sharpened through the NPM with its emphasis on a sharper distinction between politics and administration. Similarly, Kaboolian (1998) argues that an orientation to 'customer service' focuses managers and agencies on what users of the services define as important.

In view of the extended usages of the term accountability, the PhD study has used the term in its formal meaning, where it can be defined as "a relationship involving the giving and demanding of reasons for conduct" (Roberts and Scapens, 1985: p 447). It is, however, important to know about different types of

accountability relationships. Different authors have classified accountability relationships along different lines (see Table 2.4). This typology of accountabilities will be used as an analytical tool to examine the performance measurement of HMCE.

Category	Sub-category	Types	Definition
Political/public			making officials who perform public duties answerable to the people.
Managerial	<i>Fiscal/regularity</i>		making sure that money has been spent as allocated and agreed in accordance with prescribed rules.
	<i>Process</i>	<i>Economy</i>	ensuring that the best possible terms are applied in acquiring the resources. Thus, it is the input stage which comes under scrutiny under this form of accountability.
		<i>Efficiency</i>	ensuring that maximum output is obtained from the resources employed or conversely minimum resources are employed while achieving a given level of output.
	<i>Programme / effectiveness</i>		ensuring that a given course of action or investment of allocated resources results in achievement of intended objectives and goals.
Legal			scrutiny of observance of legal provisions.
Personal			moral obligations and pricks of conscience
Professional			meeting standards set by the peers of a group (e.g. ACCA or CIMA for accountants or General Dental Council for dentists)

Table 2.4: Types of accountabilities [tabulated by the PhD author from Power, 1997: p 49-50; Sinclair, 1995; Day and Klein, 1987: p 25-28; Rhodes, 1985: p 402-6]

The first major type is **political / public accountability** as the officials of public sector organisations are politically accountable to the people through indirect linkages held intact by the process of ministerial responsibility. **Managerial accountability** is concerned with the exercise of delegated authority by managers for carrying out agreed tasks according to agreed criteria of performance. This form of accountability may have a more formal technical appearance and may be carried out by impartial, neutral experts on behalf of the principals. The *economy, efficiency and effectiveness*, the three Es, are collectively also termed *Value For Money* accountability (VFM), as mentioned



earlier. Stewart (1984: p 17) distinguishes the bases of accountability in the form of a 'ladder'. '*Accounting for probity and legality*' reports that funds have been used in appropriate manner. The next level is '*process accountability*' which accounts for the details of the action processes followed by the 'agent'. '*Performance accountability*' and '*programme accountability*' together are intended to provide an account of the total work performance of the 'agent' in terms of specific goals set by the 'principal'. Finally, '*policy accountability*' complements the 'performance' and 'programme' levels presenting the account in broad policy terms in relation to the goals. In **legal accountability** the ministers and officials are held to account by judicial bodies such as courts and tribunals. The **personal accountability** concerns the domain of one's personal views of what is good and bad and to refrain from doing something bad. **Professional accountability** refers to the situation of persons who perform tasks of professional nature like doctors, lawyers, accountants. They feel accountable to their peer group for professional competence.<sup>13</sup>

Romzek and Dubnick (2000) provide a typology of accountability along two dimensions of 'sources of expectations and/or control' (internal/external) and 'degree of autonomy' (low/high). The authors argue that accountability can be built in internally or it may be carried out by an external actor. If it is internal and hierarchical in nature the managers have a low degree of autonomy. On the other

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<sup>13</sup> Stone (1995) also provides a classification of accountability mechanisms in the public sector by suggesting five types. *Parliamentary control* subjects officials to control and direction on an issue-by-issue basis. *Managerialism*, by contrast, involves setting policy and procedural guidelines then stepping back from detailed control. *Judicial or quasi-judicial review* relies on mechanisms for appeal against decisions. '*Constituency relations*' consist of various mechanisms to make organisations more responsive to their publics, from consultative committees to the Citizen's Charter. Finally, *marketisation* seeks to achieve the same end by giving clients choice among alternative service providers.



hand if it is of professionals then the managers have greater autonomy. If accountability is done externally, and is of legal nature then the managers have again little autonomy. But if it is of political nature then the autonomy is much greater. The authors state that the broken lines between cells are intended to convey the permeability of these category boundaries.

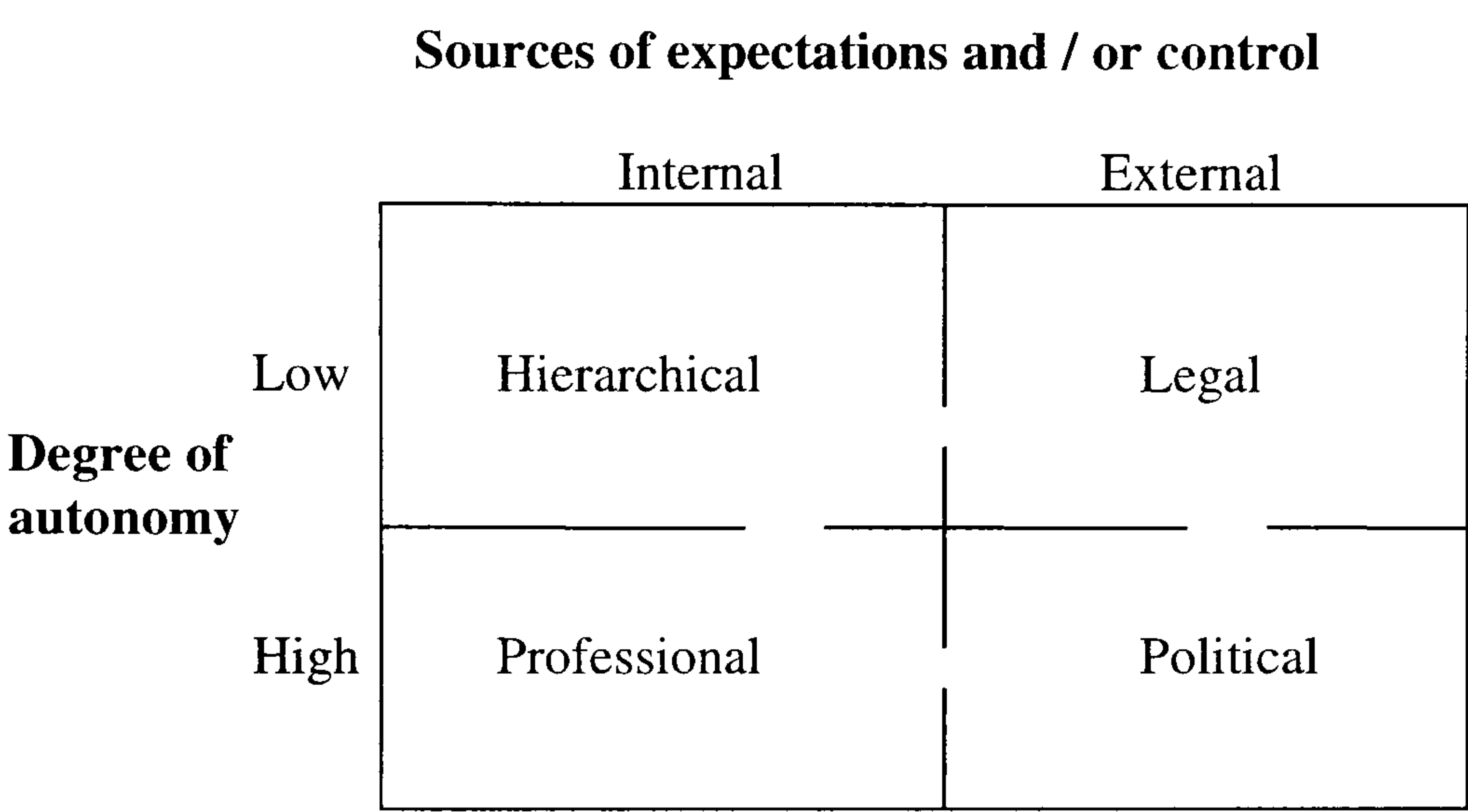


Fig 2.4: Types of Accountability Relationships (Romzek and Ingraham, 2000: p 242)

The authors argue that public sector managers are faced with cross pressures of accountabilities as the various accountability relationships emphasise different values and behavioural expectations (see fig 2.5)

Type of accountability	Value emphasis	Behavioural expectation
Hierarchical	Efficiency	Obedience to organisational directives
Legal	Rule of law	Compliance with external mandates
Professional	Expertise	Deference to individual judgment and expertise
Political	Responsiveness	Responsive to key external stakeholders

Fig 2.5: Values and Behavioural Expectations of Different Accountability Types (Romzek and Ingraham, 2000: p 242)

### **2.2.2 NPM and Accounting**

Enhancing accountability of managers was identified in the previous sections as of central importance in the NPM discourse. How can accountability be effectively operationalised is however a question which is not so well articulated in the literature. The notion of accountability at an abstract level is simple but its actual implementation is cloudy (Robinson, 2003; Collins, 1992; Swieringa and Weick, 1983).

According to Romzek and Dubnick (1998) the process of operationalisation requires establishment of expectations, verification of performance, maintaining responsiveness of agents, assessment of blame, sorting out responsibilities, determining who the masters are, and management under conditions of multiple accountability systems. Arguably all these attributes are easier said than done. The authors further argue that the growth of professionalism in the modern service delivery state has further compounded the problems of accountability, as a professional believes that he or she is accountable only to his or her peers. Despite these challenging issues, the advocates of NPM prescribe accounting as a device of making accountability process more visible (Broadbent and Guthrie, 1992). 'Performance measurement' can therefore be seen as an effort on the part of policy makers to operationalise accountability in the public sector.

A few studies have investigated the role of accounting in the process of accountability. Ahrens and Chapman (2002) observe that the relationship between accounting and processes of accountability is of vital interest to

accounting researchers as it emphasises the demanding and giving of reasons for action as the most important social function of accounting<sup>14</sup>. The NPM also appears to be placing its faith in accounting as a tool of accountability. Hood (1995) highlights the key role played in the emergence of NPM process by ‘accountingisation’. The NPM therefore is based on the notion that the activities of public servants need to be more closely appraised (in terms of costs) and evaluated by accounting techniques. (Hood, 1995: p 94; Power and Laughlin, 1992: p 133).

The issue of performance measurement in the public sector has been addressed in the literature in three main ways. First, at macro level many authors (e.g. Martin, 1998) have investigated the influence of NPM on public sector organisations. Second, they examine governmental level accounting reforms across the whole public sector (e.g. Bevir and O’Brien, 2001). Third, at micro level, many authors have examined implementation of performance measurement in an organisation or a range of organisations, on a case study basis (e.g. Greener, 2003; Laughlin et al. 1994).

To a varying degree the authors address the question as to how effective are accounting changes (such as changes in performance measures) in enhancing or modifying accountability relationships? Guided by Broadbent and Guthrie (1992), the writers can be categorised as belonging to three categories. First, the

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<sup>14</sup> They review the accountability literature and conclude that it is primarily based on narratives around bipolar distinctions between financial accountability and competing orientations. They cite examples as functional (Ahrens, 1999), professional/public service (Ashmore et al., 1989; Laughlin, 1996; Llewellyn, 1998; Kurunmäki, 1999), engineering/public service (Dent, 1991), technological/local community (Berry et al., 1985), or operational/experimental (Jönsson and Grönlund, 1988).



‘normative’ category (e.g. Kaplan and Norton, 2001; Kaplan, 2001; Chow et al., 1998; Forgione, 1997; and Carter, 1991). Such writers contend that many of the problems of performance assessment transcend the public/private distinction reflecting characteristics which cut across this divide. They are of the view that performance measurement can be used as an effective management tool by the public sector managers in the same way it is used in the private sector. In the public sector, Likierman (1993)<sup>15</sup> is a good example of such a category of writers.

Second, the ‘sceptics’ category (Talbot, 2000; Pollitt, 1986; Mayston, 1985) where the authors take their inspiration from the institutional theorists (e.g. Powell and DiMaggio, 1991; Scott 1987). The institutional theorists argue that in organisations such as government departments and agencies, whose survival depends primarily on the support of external constituents and only secondarily on actual performance, managers will implement the mandated systems in order to appear modern, rational and efficient, but will not actually use the systems for improving performance. Hyong (2002), for instance, claims that the search for ‘best practice’ in public sector management through private sector practices has taken on ‘mythic proportions’. The author laments the fact that the managerial, organisational, financial, legislative or policy-driven approaches are keenly

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<sup>15</sup> He draws twenty lessons from his review of Performance Indicators (PIs) used in the government departments and classifies them into four categories. The first category relates to *Concept*, which should address issues like all organisational elements, appropriate number, safeguards and accountability. The second category is that of *Preparation* which includes issues like *Ownership*, *Avoiding short-termism*, *Reflecting effort* and *Thinking about uncontrollables*. The third category of *Implementation* relates to issues like *Revision*, *Linkages*, *Understandability*, *Use as proxies* and *reassessment*. The final category of *Use* includes issues like *Trusted data*, *Guidance Feedback*, *Trade-off* and *User-friendliness*.

pursued in the literature even though they have largely failed to deliver the sweeping improvements those organisations initially expected. Ittner and Larcker (1998) stress that instead of embracing performance measurement in the public sector as a matter of belief, its applicability must become a research question which should aim at answering whether mandated PMSs are actually used for internal decision making and performance evaluation or are simply implemented to legitimate the government departments with the legislatures and other stakeholders?

Third, the ‘rationalists’ category (e.g. Broadbent and Laughlin, 1998; Power, 1997) where the authors take the middle approaches. They are of the view that accounting changes may have no effect upon the practices of an organisation if these are decoupled or marginalised. However, they may also, in some cases, transform the basic values of the organisation if they have the colonizing effect.

The rationalists and sceptics have produced literature that has been termed as the ‘alternative research’ by Broadbent and Guthrie (1992). This PhD case study investigates the use of performance measurement for enhancing and ‘modifying’ accountability relationships in the case of HMCE. It therefore falls within the umbrella term of ‘alternative research’.

During the review of literature pertaining to performance measurement it transpired that there exists wide variation in the meanings of fundamental terms



used by various authors<sup>16</sup>. It is therefore important for sake of clarity that important terms like performance measurement, performance management, PMS, performance measures and performance indicators (PIs) are defined for the purpose of this PhD study.

Neely et al. (1995) define ‘performance measurement’<sup>17</sup> as *the process of quantifying the efficiency and effectiveness of an action*. It is argued by the authors that the level of performance a business attains is a function of the *efficiency* and *effectiveness* of the actions it undertakes. The term *effectiveness* used in the definition refers to the extent to which customer requirements are met, while the term *efficiency* is a measure of how economically the firm’s resources are utilized when providing a given level of customer satisfaction. The authors stress the importance of the distinction and contend that it not only identifies two fundamental dimensions of performance, but also highlights the fact that there can be internal as well as external reasons for pursuing specific courses of action. ‘Performance Management’<sup>18</sup> is broader in meaning and is

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<sup>16</sup> Lack of clarity on usage of terms in performance related literature is well documented. For instance Neely et al., (1995) express their concern over the fact that the writings of many authors on organisational performance have an implied assumption that the term performance is well understood by all. The authors argue that the performance measurement literature is diverse where individual authors have tended to focus on different aspects of PMS design. However, the borders between the definition of the terms and concepts are often not well defined and consensus upon meaning and scope of performance management and measurement in both literature and practice is conspicuously missing (Lapsley and Mitchell, 1996).

<sup>17</sup> CIMA( 2000) defines *performance measurement* as:

“The process of assessing the proficiency with which a reporting entity succeeds, by the economic acquisition of resources and their efficient and effective deployment, in achieving its objectives. Performance measures may be based on non-financial as well as financial information.”

<sup>18</sup> Just as is the case with the term ‘performance’, the terms *performance measurement* and *performance management* are also often used in taken for granted meaning. For instance, in the official publications of government departments like Cabinet Office and NAO, the terms performance management and performance measurement have often been interchangeably used



often used more loosely by practitioners and authors implying a generic sense. Molleman and Timmerman (2003) review various definitions of ‘performance management’ as used in the published literature and observe that what is common in most of these and other definitions is that they relate ‘performance management’ with different organisational levels (organisation, unit, group, individual worker) and refer to a cyclical process with different stages, such as planning, appraisal and reward. The authors, however, contend that such definitions differ in their focus as the literature on general management and production management emphasises the organisational or unit level of performance, while HRM literature primarily focuses on the individual worker.

Williams (1998) is of the view that three perspectives on performance management are distinguishable: individual performance, organisational performance and an integration of the two. However authors of performance management point out that despite the contention that objectives must be coherent throughout an organisation, the relations between individual and organisational objectives and targets has generally been accorded less concern (Bach, 2000; Hansen, 2000; Storey and Sisson 1993).

From the public sector perspective Harry (2002) defines ‘performance management’ as the use of performance information to affect programs, policies

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e.g. performance management has been defined in a joint publication issued by the Cabinet Office and NAO in the following tautological manner:

“Performance management can refer to managing the performance of an organisation or an individual” (HM Treasury., 2001a; p 7)

Talbot (2000) provides numerous examples of the confusion which characterises the variant policy pronouncements issued by the central government policy managers over the issue of performance improvement.

or any other organisation actions aimed at maximizing the benefits of public services. It is worth recalling that the focus of this PhD research is upon ‘performance measurement’ which is seen as an important tool of performance management.

Neely et al. (1995: 80) define a ‘performance measure’ as “*a metric used to quantify the efficiency and/or effectiveness of an action*”. Fry (1992) describes ‘measures’ as a means of tracking. Nanni et al. (1990) use the analogy of a thermostat to explain how performance measures are part of a feedback loop, which “controls operations against a specific value”.

When it is not possible to measure an activity (as the phenomenon may be intangible or too complex to be defined by simple measures) some proxy is used which indirectly reflects progress achieved on the desired activity. This proxy measure is termed a ‘performance indicator’<sup>19</sup> (PI), and is often used interchangeably with performance measure. Peursem, et al. (1995) refer to Culyer, (1983, p 11) and Holland, (1983, p 53) and insist that performance measures<sup>20</sup> reported to the public should be viewed as no more than indicators, as indicators are not associated with precision or reliability, but exist to focus attention towards an issue of interest. The authors contend that PIs are useful if

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<sup>19</sup> Carter et al. (1992) classify the use of PIs as prescriptive or dials which are linked to objectives and targets set by ministers or managers and used to monitor progress towards their achievement, descriptive or tin-openers which simply record change, or proscriptive or alarm-bells which give warning about intolerable things.

<sup>20</sup> In the literature often the phrase Performance Measurement System (PMS) is used to examine the performance measures, indicators employed for measuring organisational performance. PMS is defined by Neely et al. (1995: 81) as *the set of metrics used to quantify both the efficiency and effectiveness of actions*. The authors further state that a PMS can be examined at three different levels. First, the individual performance measures; second, the set of performance measures – the PMS as an entity; and third, the relationship between the PMS and the environment within which it operates.



they inspire further enquiry, but indicators cannot be expected to stand alone as a source of information.

### **2.3 Stakeholder Theory and Performance Measurement**

In the preceding sections the central importance of accountability for NPM inspired reforms was underscored where accountability in its formal sense was defined as a relationship involving the 'giving and demanding of reasons for conduct'. The principal-agent approach models the interaction between two sets of people, the 'principal' on the one hand and the 'agent' on the other hand (Ricketts, 2002). The one who demands accounts is the principal while the one who gives accounts is the agent (Laughlin, 1996; Mayston, 1993). Consequently the question of how the principal defines *performance* becomes important as the nature of *accounts* will depend on the notion of performance. A review of the literature on performance measurement suggests that the notion of performance has steadily evolved to accommodate more than one perspective.

Tracing the development of management accounting, Anthony (1989: 5) claims that customarily 'performance' was construed around a plant or a business unit. The research in the mid-1980s began to focus on the manufacturing planning and control system. Kaplan (1983) is thought to be among the first ones who highlighted the shortcomings of traditional cost accounting in today's manufacturing environment. Authors like Fry and Cox (1989) also challenged the operating assumptions made by traditional cost accounting and proposed new PMSs based on theory of constraints. Lockamy and Spencer (1998) further state



that while some researchers (e.g. Schonberger, 1990) focused on individual performance measures and examined various dimensions of quality, cost, time and flexibility from a strategic perspective, others (e.g. Kaplan and Norton 1992; Dixon et al. 1990, Fitzgerald et al., 1991) developed frameworks for relating functional or local performance to overall business level performance. In the Table 2.5, important frameworks are summarised.

No	Frameworks	Originators / Authors	Focal Point
1	Pyramid of financial ratios	Donaldson Brown and DuPont cousins in 1912	Explicit hierarchical structure, linking measures at different organisational levels.
2	Performance Measurement Matrix	Keegan et al. (1989)	categorises measures as being 'cost' or 'non cost', and 'external' or 'internal', reflecting the need for greater balance of measures across these dimensions.
3	SMART (Strategic Measurement and Reporting Technique) pyramid	Lynch and Cross (1991)	internally and externally focused measures, cascading measures down the organisation so that measures at department and work centre level reflect the corporate vision
4	Results and Determinants Framework (RDF)	Fitzgerald et al. (1991)	classified measures into two basic types; relating to results (competitiveness, financial performance) and to determinants of those results (quality, flexibility, resource utilisation and innovation).
5	Macro Process Model of the Organisation	Brown (1996)	Clear links between five stages in a business process, <i>Inputs, Processing System, Outputs, Outcomes</i> and <i>Goals</i> , and their performance measures;
6	Balanced Scorecard	Kaplan and Norton (1992 and 1996).	identifies and integrates four different ways of looking at performance (Financial, Customer, Internal Business and Innovation and Learning Perspectives).
7	Tableau de Bord	A French PM system	establishes a hierarchy of interrelated measures and cascading measures to different organisational levels, forcing functions and divisions of an organisation to position themselves in the context of the company's overall strategy.
8	The Performance Prism	Neely et al.(2000)	stakeholder centric view of performance measurement. In addition to stakeholders like, shareholders investors, customers, employees and suppliers the Prism also considers regulators and pressure groups.

Table 2.5: Important performance measurement frameworks (tabulated by the PhD author)

In the early 1990's, authors such as Fitzgerald et al, (1991) and Kaplan and Norton (1992) began criticising the traditional emphasis on financial measures of performance like profit margin and return on investment (ROI). These advocates of a multidimensional PMS argued that financial measures promoted short-termism which might endanger long term sustainability of a business organisation. They therefore argued for expanding the notion of performance by dissecting it into its constituent elements such as results and determinants under Fitzgerald et al and drivers of performance under Kaplan and Norton's Balanced Scorecard. Yet another push for expanding the notion of performance came from the advocates of stakeholder theory. Freeman (1984) argued that many groups and individuals (besides shareholders) can affect an organisation, and thus there was a need to respond effectively to all those groups and individuals<sup>21</sup>. The stakeholder approach influenced many disciplines including management accounting as Neely et al. (2000) propose the 'Prism framework' which draws its inspiration from the stakeholder theory and argues that an organisation's results (stakeholder satisfaction) are a function of determinants (the other Prism facets)<sup>22</sup>.

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<sup>21</sup> Admittedly the stakeholder theory has not met with universal approval and many critics continue to express their preference for shareholders as the only legitimate Principal and contend that the accounts should reflect the shareholders' views of performance (e.g. Sundaram and Inkpen, 2004). However the theory has left an impact upon various disciplines of strategic management.

<sup>22</sup> The authors propose five facets of performance prism in the form of following questions:

- Stakeholder Satisfaction – who are our key stakeholders and what do they want and need?
- Strategies – what strategies do we have to put in place to satisfy the wants and needs of these key stakeholders?
- Processes – what critical processes do we need to operate and enhance these processes?
- Capabilities – what capabilities do we need to operate and enhance these processes?
- Stakeholder Contribution – what contributions do we require from our stakeholders if we are to maintain and develop these capabilities?



It follows from the preceding sections that the NPM model of private sector managerial practices rests on a firm belief that in the private sector performance is improved with the use of accounting practices. However even within the body of literature related to private sector there is a recognition of the fact (as indicated by multi dimensional performance frameworks, and the accounting theories inspired by the stakeholder theory) that *performance* is a contested notion and maybe construed differently by various stakeholders of an organisation. Interestingly NPM steers clear of such debates on the efficacy of using accounting information in the private sector. Many writers have referred to the complexities and limitations related to using the accounting information as a part of an accountability system. For instance Roberts and Scapens (1985) contend that a better understanding is required of the way in which accounting systems become embodied, through use in organisational systems of accountability. It is therefore interesting to examine how performance measurement works as a mechanism of accountability in the case of public sector where stakeholders are more numerous and the resulting accountability system more complex (Brignall and Modell, 2000). The case of HMCE is also interesting as the main service (i.e. tax collection) is viewed differently by various stakeholders. The notions of accountability, performance, performance measurement, and performance indicators need to be viewed from the perspectives of both the tax collectors and tax payers. In order to develop a framework for analysing the evidence in the case of HMCE the most important theoretical underpinnings of the PhD research are discussed next.



### **2.3.1 The Theoretical Underpinnings**

This PhD research collects evidence from various textual sources and then analyses it to answer the main research question. In order to develop analytical tools the research has drawn insights from a few theoretical frameworks. The importance of stakeholder theory with respect to accountability system of a public sector organisation has already been mentioned in the previous section. The other important theoretical underpinnings of this research have been obtained mainly from institutional and structuration theories and the principal-agent model of accountability.

Earlier it was argued that the sceptics question the assumptions of normative writers with regards to NPM-inspired accounting changes. For instance, Lapsley (1996) is not very convinced by the checklists of Likierman (1993) for designing and implementing PIs and regards their usage as clumsy which do not address the finer requirements of professional value systems of the public sector organisations.

Both sceptic and rationalist authors have used the theoretical framework of *institutional theory* to analyse the process of accounting changes in public sector organisations. While the sceptics (e.g. Kurunmaki et al., 2003) have used the institutional theory based frameworks to challenge the claims of NPM regarding accounting as a force of change, the rationalists (e.g. Collier, 2001, Burns, 2000) have used the framework for analyzing the process of accounting changes and the resulting reactions from the managers and other employees of an organisation.

‘Institutional theory’ itself is not a single theory but is rather an umbrella term for the contributions of various authors from different disciplines (Scott, 1987). The theory tries to dig deeper into the foundations of social structures. It looks into the processes by which structures, including schemas, rules, norms, and routines, become established as authoritative guidelines for social behaviour (Scott, 2004: p 408). The various variants of *institutional theory*<sup>23</sup> like ‘Old Institutional Economics’ (OIE), ‘New Institutional Economics’ (NIE) and ‘New Institutional Sociology’ (NIS) have their roots in different disciplines like economics, political science and sociology (Burns, 2000: p 571). Kondra and Hinings (1998) refer to the variety of guises of *Institutional theory* and identify the central thrust of the NIS is to explain the isomorphism of organisational fields (i.e. organisations in a particular field gradually become similar) and the establishment of institutional norms. While the historical past of an organisation accounts largely for ‘institutions’ of an organisation, the NIS writers argue that some external pressures ensure conformity to norms. They identify these pressures as ‘coercive isomorphism’ (the pressure comes from a superior organisation), ‘mimetic isomorphism’ (where an organisation, finding itself in doubt, copies what the perceived leaders of the field are believed to be doing) and ‘normative isomorphism’ (where an organisation, is heavily influenced by

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<sup>23</sup> Scott (2004), one of the proponents of institutional theory, provides a good description of how the theory has developed over the years. He encapsulates the theory in the following lines:

“institutional theory is broadly positioned to help us confront important and enduring questions, including the bases of organisational similarity and differentiation, the relation between structure and behaviour, the role of symbols in social life, the relation between ideas and interests, and the tensions between freedom and order” (p 2)



norms set by an external body) (Powell and DiMaggio, 1991; DiMaggio and Powell, 1983).

This PhD research analyses the NPM-inspired accounting reforms aimed at bringing about a fundamental change in the ethos of HMCE. The NIS framework was, therefore, found to be the most relevant one as various external factors can be examined and analysed for their influence upon the accounting based accountability relations in HMCE.

‘Institution’ is a key concept of many fields of social sciences. Scott (1995: 33) defines the focal term as used in sociology as:

“Institutions are social structures that have attained a high degree of resilience. [They] are composed of cultural-cognitive, normative, and regulative elements that, together with associated activities and resources, provide stability and meaning to social life. Institutions are transmitted by various types of carriers, including symbolic systems, relational systems, routines, and artefacts. Institutions operate at different levels of jurisdiction, from the world system to localized interpersonal relationships. Institutions by definition connote stability but are subject to change processes, both incremental and discontinuous”...

Scott in the above definition identifies three pillars of *institutions* which he also presents in the form of a table as:

	Regulative	Normative	Cognitive
<i>Basis of compliance</i>	Expedience	Social Obligation	Taken for granted
<i>Mechanisms</i>	Coercive	Normative	Mimetic
<i>Logic</i>	Instrumentality	Appropriateness	Orthodoxy
<i>Indicators</i>	Rules, laws, sanctions	Certification, accreditation	Prevalence, isomorphism
<i>Basis of legitimacy</i>	Legally sanctioned	Morally governed	Culturally supported, conceptually correct

Table 2.6 Three pillars of institutions (source: Scott, 1995: p 18)



Powell and DiMaggio (1991:8) provide the NIS based description of 'institutions' which carry some commonality with the more general definition but has a greater focus upon explaining a social phenomenon by referring to many external factors:

"The new institutionalism in organisation theory and sociology comprises a rejection of rational-actor models, an interest in institutions as independent variables, a turn toward cognitive and cultural explanations, and an interest in properties of supra-individual units of analysis that cannot be reduced to aggregations or direct consequences of individuals' attributes or motives".

It is argued that organisational environments "*...are characterized by the elaboration of rules and requirements to which individual organisations must conform if they are to receive support and legitimacy ...*" (Scott and Meyer, 1983: 149).

The main contention of the institutional theorists is that the taken for granted norms<sup>24</sup> and values of an organisation define the operational life of an organisation. How are those norms developed? Answering this question Stinchcombe (1965) popularised the notion of *organisational imprinting* as he argued that organisations formed at one time typically have a social structure which gets *imprinted* on the organisational psyche. The notion of *organisational imprinting* as a process by which organisations tend to maintain certain practices adopted at the time of origin of that organisation is important for HMCE and will be used for analysis in the later chapters

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<sup>24</sup> According to Hinings and Greenwood (1988):

"...institutional norms deal with appropriate domains of operation, principles of organizing, and criteria of evaluation. Structures and processes are institutionally derived and may even be idiosyncratic to the organisational field"

### **2.3.2 Responses to Accounting Changes**

When the *sceptics* apply the institutional theory lens for analyzing accounting changes they consider such changes as an exercise in gaining legitimacy. A very good example of this approach can be found in Kurunmaki et al. (2003) where the authors pitch the analysis of the accounting changes in the healthcare as a contrast between *accountingisation* and *legitimation*. Carpenter and Feroz (1992) also use this theoretical lens to view adoption of GAAP in the public sector as an attempt to be seen legitimate and modern. Power (1997: 67) refers to the cosmetic nature of accounting changes and contends that:

“through the creation of compartmentalized organisational units for dealing with external assessment, audit and evaluation can be rendered ceremonial in such a way as to deflect a rational questioning of organisational conduct”.

While the *sceptics* term this phenomenon as ‘decoupling’, *rationalists* point out the norms distorting effects of accounting changes basing their analysis on the dictum that ‘*what’s measured gets done*’. They term it the ‘colonising’ effect where formal audit based accountability may penetrate deep into the core of organisational operations creating ‘new mentalities, new incentives and perceptions of significance’ (Broadbent and Laughlin, 1998: p 405). Pollit (1995:142), for instance, argues that quality audits of academics has resulted in academics reluctantly resorting to some least desired actions like cutting per student class contact times, teaching much larger classes, reducing the number or length of written assignments, sacrificing time for research and scholarship and so on. Broadbent and Laughlin (1998) conducted semi-structured interviews of teachers and head teachers in 24 schools and staff of 34 GP practices for an analysis of their coping strategies in the wake of performance reporting changes.



They reported that while decoupling occurred in the case of GP practices, colonising effect was visible in the case of schools.

Scott (2004) himself recognises the weaknesses of a two-fold simplistic view of responses towards organisational changes (including accounting changes). Many writers using insights of institutional theory have tried to improve the robustness of the NIS based analytical tools. For instance, Collier (2001) shows how accounting in the form of devolved budgets facilitated ‘loose coupling’, by accommodating both institutional and technical demands. He claims that the devolution of budgets in West Mercia Police was accompanied by a shift in power that helped to reconcile the interests of those pursuing a legitimating accountability with those who prioritized operational policing.

Roberts and Scapens (1985) and Macintosh and Scapens (1990) emphasise the importance of ‘structuration theory’ of Giddens (1984) in understanding the social context of management accounting in organisations. Structuration<sup>25</sup> theory is concerned with understanding the relationship between the activities of knowledgeable human actors and the structuring of social systems (Giddens, 1979, 1984). It can be argued that Giddens’ structuration theory attempts to synthesise the views that either consider social phenomena as determined by the influence of objective social structures (determinism) or consider social phenomena as products of human agents as they subjectively interpret the world (voluntarism). For Giddens, social systems comprise discernibly similar social

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<sup>25</sup> According to Giddens (1984:: 376) ‘structuration’ is “the structuring of social relations across time and space, in virtue of the duality of structure”.



practices which are reproduced across time and space through the actions of human agents, while structure refers to the structuring properties which provide for the “binding” of those social practices into social systems’ (Macintosh and Scapens, 1990: 457) It is only through action and interaction that structures are themselves reproduced. This is Giddens’ notion of the duality of structure whereby structures are both the medium and the outcome of interaction.

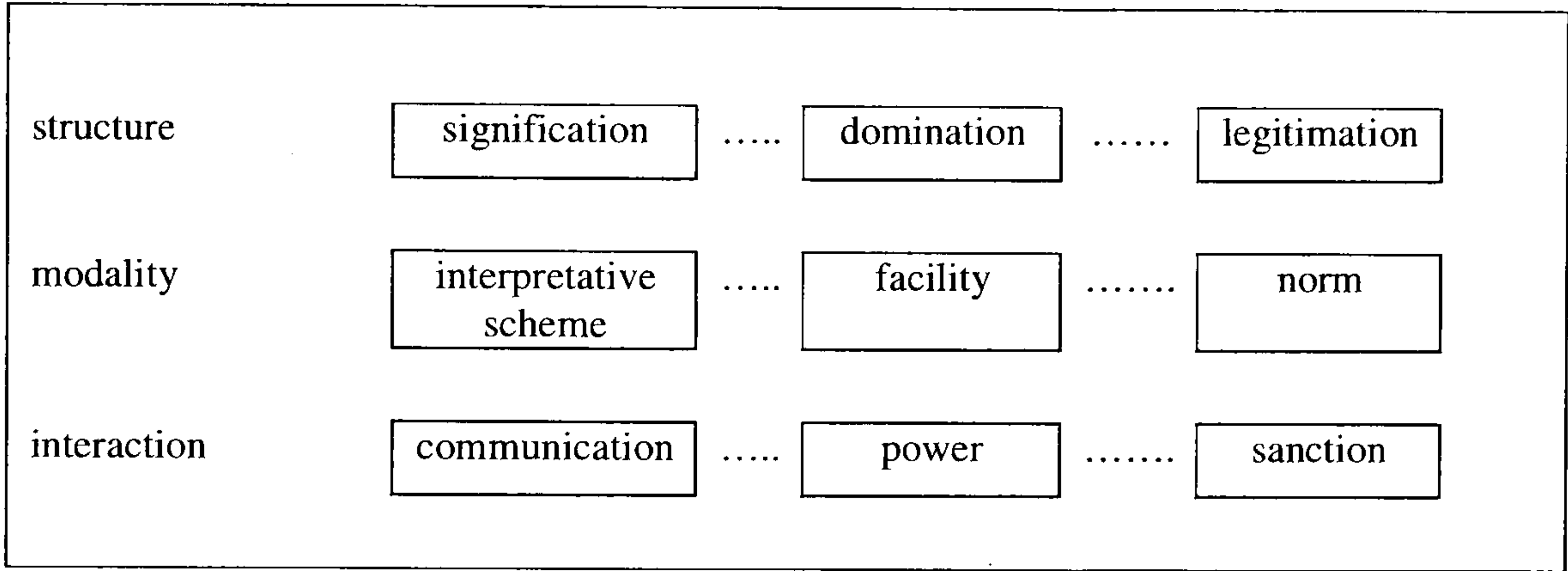


Fig 2.6 : Giddens’ Structuration Framework (Giddens, 1984: p 29;  
Source: Macintosh and Scapens, 1990)

According to Macintosh and Scapens (1990) management accounting provides managers with a means of understanding the activities of their organisation and allows them to communicate meaningfully about those activities therefore management accounting systems can be thought of as a *modality* of structuration theory. As such insights from structuration theory are helpful in developing a framework for analysing the accountability system of HMCE.

Laughlin (1991) uses insights of *institutional theory* and *structuration theory* to present effects of changes (such as accounting changes) in terms of responses by managers of an organisation. He conceptualizes organisations as being an

amalgam of “interpretive schemes”, “design archetypes” and “sub systems”. The nature and relationships between these is shown in Figure 2.7

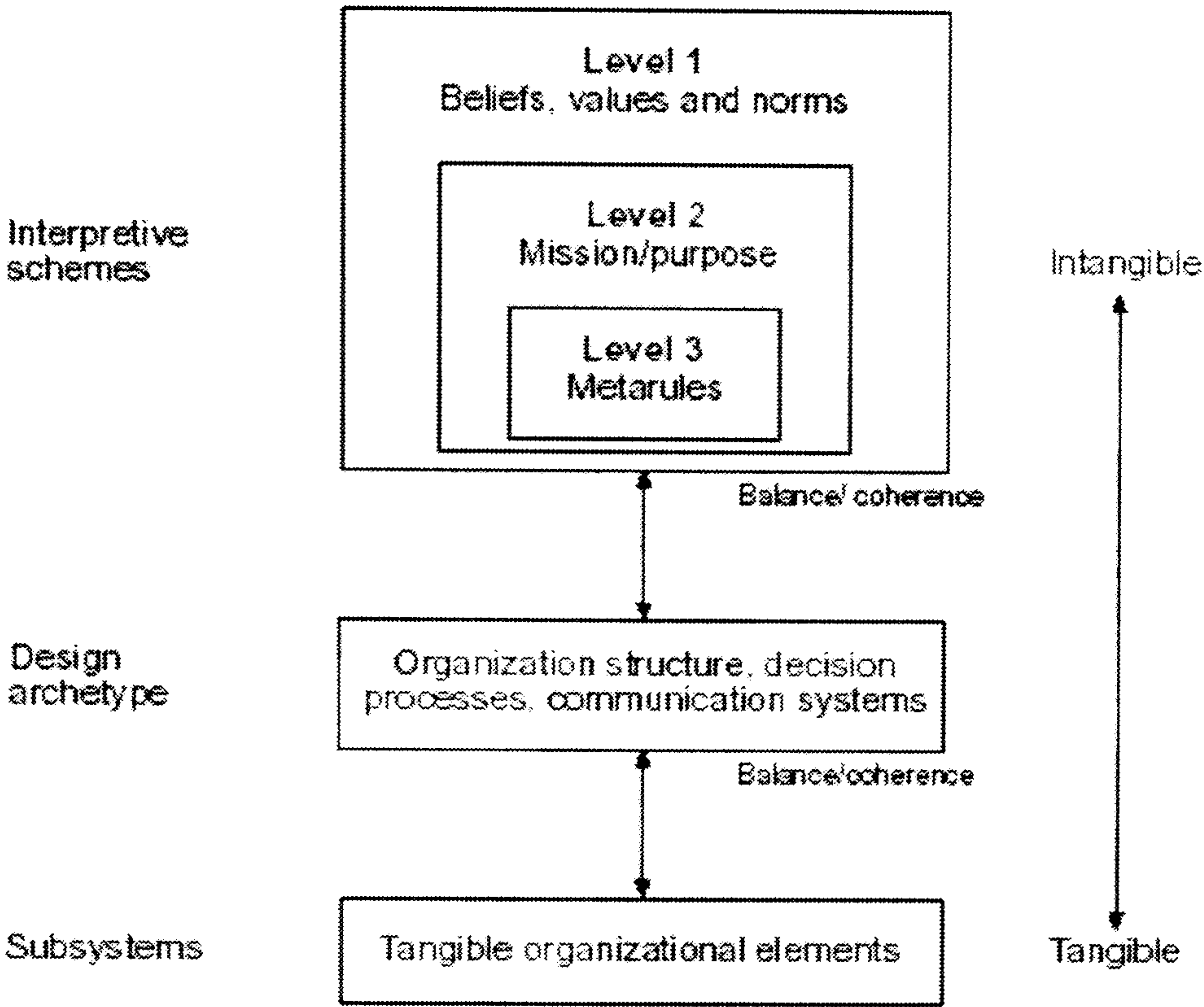


Fig 2.7: A model of organisations (Source: Laughlin, 1991: p 211)

The figure shows that the interpretive schemes of Laughlin’s framework are shaped by assumptions or beliefs which organisations tend to maintain as they are imprinted from the times the organisation was founded and as such they are taken for granted set of shared values and beliefs (Hinings and Greenwood, 1988: p 4). Referring to the Habermesian Critical Theory, Laughlin (1991) categorises different constituents of an organisation along a continuum of tangible to intangible elements. The tangible elements (e.g. buildings, people, machines, finance and the behaviours and natures of these elements) are those about which inter-subjective agreement is possible and the less tangible ones are those which give direction, meaning, significance, nature and interconnection to



the more tangible elements and about which inter-subjective agreement is very difficult. This less tangible part is divided into two progressively less visible parts:

- a design archetype and
- interpretive schemes,

Both of them are created and sustained by the past and/or current organisational participants. The definition for a *design archetype* is borrowed by the author from Hinings and Greenwood (1988: 4):

“...compositions of structures and (management) systems given coherence and orientation by an underlying set of values and beliefs”

The underlying set of values and beliefs are termed *interpretive schemes*.

Drawing upon works of many scholars of organisational change, Laughlin (1991) conceptualizes four possible pathways which any change initiative may follow. The first two pathways have been termed *First-order changes* and include Rebuttal and Reorientation. In the case of *Rebuttal* there is a repulsion of the disturbance such that, while the eviction may involve some change in the organisational arrangements, these are very temporary. Reorientation, on the other hand, aims to internalize the disturbance, through often permanent organisational changes, but in such a way that the *interpretive schemes* remain untouched and undisturbed by the alteration. The next two reactions are categorised as *Second-order changes* comprising Colonization and Evolution. When a change results in *colonization* the change is deep-rooted as the design archetype, the subsystems and the interpretive schemes of the organisation all undergo complete transformation. This change in the interpretive schemes results

in a totally new underlying ethos for the organisation as a whole. *Evolution* on the other hand, involves deliberately chosen change in the interpretive schemes, with subsequent shifts in the design archetype. Thus such a change results from general acceptance by all the organisational participants freely and no external coercion is involved.

Laughlin stresses that these four possibilities are simply heuristic devices to provide a framework of possibilities and suggests that actual pathways of change may move dynamically and will not necessarily follow a linear, one-directional course. There may be oscillations on a pathway, or different sections of an organisation may progress at different paces, on different pathways, or in contradictory ways (Broadbent, 1992).

Oliver (1991: 152) also provides a continuum of responses to institutional pressures, which is used by Modell (2001: 440) for analysing accounting based reforms.



A continuum of managerial responses to institutional pressures. Source: adapted from Oliver (1991, p. 152)

Level of active resistance to institutional pressures.			
	Strategies	Tactics	Examples
	Acquiescence	Habit	Following invisible, taken-for-granted rules
		Imitate	Mimicking institutional models
		Comply	Obeying rules and accepting norms
	Compromise	Balance	Balancing the expectations of multiple constituents
		Pacify	Placating and accommodating institutional elements
		Bargain	Negotiating with institutional constituents
	Avoid	Conceal	Disguising non-conformity
		Buffer	De-coupling structural elements
		Escape	Changing goals, activities or domains
	Defy	Dismiss	Ignoring explicit norms and values
		Challenge	Contesting rules and requirements
		Attack	Assaulting the sources of institutional pressure
	Manipulate	Co-opt	Importing influential constituents
		Influence	Shaping values and criteria
		Control	Dominating institutional constituents and processes

The responses can vary from very low to very active resistance to accounting reforms. At the low resistance end of the continuum the strategy will be of *acquiescence* while at the active resistance end the strategy will be of *manipulation*.

From the preceding discussion on institutional theory three important insights can be drawn. First, an organisation is given coherence and stability by *institutions* (which are internalized definitions of how routines should be done, and how events are interpreted by the managers and employees of an organisation). Second, pressures upon an organisation to undertake reforms can emerge from a regulating authority (coercive pressure), from a norms-setting body (normative pressure), or from leaders of the field (mimetic pressure). Third,

how managers respond to such pressures for reforms can vary from simple acquiescence to manipulation.

Institutional theory has been applied to case study-based research by some authors (e.g. Covalleski and Dirsmith, 1988; Kikulis, Slack, and Hinings, 1995).). However, many authors have argued that given the importance of the institutional theory, it is still underutilized. For instance, Collier (2001) refers to the calls for studies of accounting in the context in which it operates (e.g. Hopwood and Miller, 1994, Hopwood, 1990, 1987, 1983; Burchell et al., 1980) to justify the choice of institutional theory as the framework for his study. Brignall and Modell (2000: 282) regard the neglect of the insights of institutional theory in the context of the public sector as ‘unfortunate’ and call for shifting the attention to “*the power and pressures exerted by different groups of stakeholders and how these affect the use of performance information in organisations*”. This PhD study addresses such calls by employing insights drawn from institutional theory for analysing the NPM-inspired performance measurement changes which aim to alter accountability relationships in HMCE.

Earlier it was stated that the main thrust of NPM can be identified as redefining accountability in terms of ‘customer-focus’. It was also stated that in the case of a ‘tax administration’ the notion of ‘customer-focus’ is not well developed. In order to develop such a notion ‘social exchange’ theory (with its origins in anthropology and sociology) (Ekeh, 1974; Turner, 1982) is very helpful. Alford (2002) makes a good review of the theory as to how it can resolve some of the problems associated with the adoption of a private-sector-style customer-focus in the public sector. The author argues that the interactions between public-sector



organisations and their clients differ from the private-sector customer transaction and offers a typology of these interactions. The notion of ‘*exchange*’ in the social exchange theory has two important features. First, it acknowledges that it is not only tangible items such as money or goods and services which can be exchanged, but rather a broader set of exchangeable things such as friendship, respect, or affirming fairness. Second, ‘social exchange’ can involve more than two parties and more complex forms of ‘reciprocity’. As against "restricted exchange" occurring between only two parties in the private sector, Levi-Strauss ([1949] 1969, p: 220) identifies another form as a "generalized exchange", which involves actors who benefit each other indirectly" (Ekeh 1974, p: 48).

Alford (p 341) further states that these two aspects of social exchange typically entail more diffused and deferred reciprocity than a simple economic exchange. After explaining the notion of social exchange, the author offers a typology of *organisation-public* relationships based on a primary distinction between ‘citizens’, who receive public value from the public sector organisations and ‘clients’ who have their private value affected and with whom an organisation deals directly as part of normal business operations. Within that category, a secondary distinction is drawn among three roles: ‘paying customers’, ‘beneficiaries’, and ‘obligatees’. The author states that in this typology, only the paying customer seems to conform to the private-sector market model but that role is always mixed with some other that does not conform. The broadened

conception of exchange suggests recognition of *beneficiaries* and *obligatees* as clients, even though they are not the same as paying customers<sup>26</sup>.

The *obligatee* as a non-paying customer identified by the author is important for the case of HMCE as this type of client usually receives what he or she reasonably regards as ‘*bads*’ under social exchange theory. A prisoner, the author illustrates, mainly receives the restraint of liberty. Since a prison is not seeking to obtain repeat business, therefore achieving satisfaction of inmates as the first objective and thus calling *obligatees* clients may appear misplaced. However referring to the social exchange notion, the author contends that an *obligatee* provides not money but *compliance* which is essential for the organisation's requirements. The organisation is seeking not repeat sales but ongoing compliance, without which it cannot effectively function. Even though compliance can be obtained through coercion, such a course is often very costly, especially if the *obligatees* are wilfully resistant.

“The challenge, therefore, is to elicit from them some degree of cooperation with the agency. This means understanding obligatees’ needs and rights and seeking to satisfy them to the extent it can do so, given its primary responsibility to impose legal obligations” (p 343)

Citing the need for fairness and justice as a primary desire of *obligatees*, the author claims that considerable research evidence suggests that most people will comply with legal sanctions, even if they are personally disadvantaged by doing

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<sup>26</sup> The author illustrates the point by using welfare payments as an example. He states that beneficiaries, e.g. welfare recipients, receive benefits from the agency not because the agency will get money in return, but rather to fulfil a mandate endowed upon it through the political process by the citizenry. The citizenry receives public value in return for the authority and resources it bestows on the agency. First, it receives a kind of social insurance by feeling reassured that a safety net is present. “It also receives a mitigation of negative externalities in that people who have some form of income support are less likely to engage in theft or to sleep in the doorways of middle-class taxpayers.” Refraining from acts of rebellion on the part of recipients and affirmation of normative and symbolic values like human rights of the under privileged are cited as some other examples of values received by the citizenry (p 342)



so, if they regard the manner in which those sanctions are applied as fair (Tyler 1990; Ayres and Braithwaite 1992).

The author recognizes that there will always be some proportion of *obligatees* who are wilfully resistant, requiring use of coercive powers against them. However that falls outside the scope of exchange; the *obligatees* don't receive anything valuable, but rather find the value they enjoy diminished<sup>27</sup>. Using the prison example, the author argues that very rarely a specific person is solely a *beneficiary* or an *obligatee* as quite often such a person plays both of these roles at the same time. For instance, the welfare recipients in one way are *beneficiaries*, but at the same time they are also *obligatees* because services to *beneficiaries* are rationed using eligibility criteria, which the welfare department has to enforce. To the extent they are subject to these rules, benefit recipients are also *obligatees*. While the agency can apply coercive powers, such as inspections and prosecutions, to detect and punish "welfare cheats." but it is also desirable to understand the factors that make it difficult for some beneficiaries to comply- such as lack of information or complex procedures-and by addressing them try to make it easier for clients to comply. The author concludes from the example that compliance can be elicited from *beneficiaries* and *obligatees* by treating them

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<sup>27</sup> It is argued by the author that by engaging with those who are not wilfully resistant in the process of exchange, the agency also participates in exchange with the citizenry. The author contends that in return for their authority and resources, the agency provides them with public value. "*In general, this public value consists of compelling members of society to act consistently with laws, which are usually enacted in order to enhance public value. It also includes providing the means to punish breaches of such laws*". From the operation of a prison, the citizenry receives a guarantee that its laws have teeth, as well as reassurance that dangerous offenders are kept out of the community while they are a threat to society and the prospect of rehabilitating them. It also receives normative value in the form of affirmation that its prisons exhibit the attributes of a fair and just society in the manner of their operation. Thus, the prison agency is engaged in exchanges both with the citizenry and with its inmates (p 343)

like customers. This theme will be used while analysing the PMS of HMCE with the help of *Results and Determinants Framework* (RDF) in the later chapters.

## **2.4 Theorising Accountability**

Earlier, accountability was defined as ‘giving and taking of reasons for conduct’. Since accountability itself is an abstract notion, some authors have proposed graphical presentation of how it operates. The principal-agent model was referred to in earlier sections. The principal-agent model originated as a theoretical construct in the new economics of organization to examine contractual and hierarchical relations between actors within the firm. It not only continues to be an important framework for the analysis of a broad range of relationships in economics (Moe 1984: 739) but has often been applied for analysing accountability relationships in the public sector as well (Mayston, 1993). Laughlin (1996) presents the principal-agent model of accountability in a simple diagram (Fig 2.8) where the principal provides resources/responsibilities to the agent and thereafter places demands upon the agent for information as to how the resources were utilised or responsibilities performed? The agent in compliance supplies the information on his activities so that the principal is satisfied with the performance of agent and the accountability relationship remains intact.



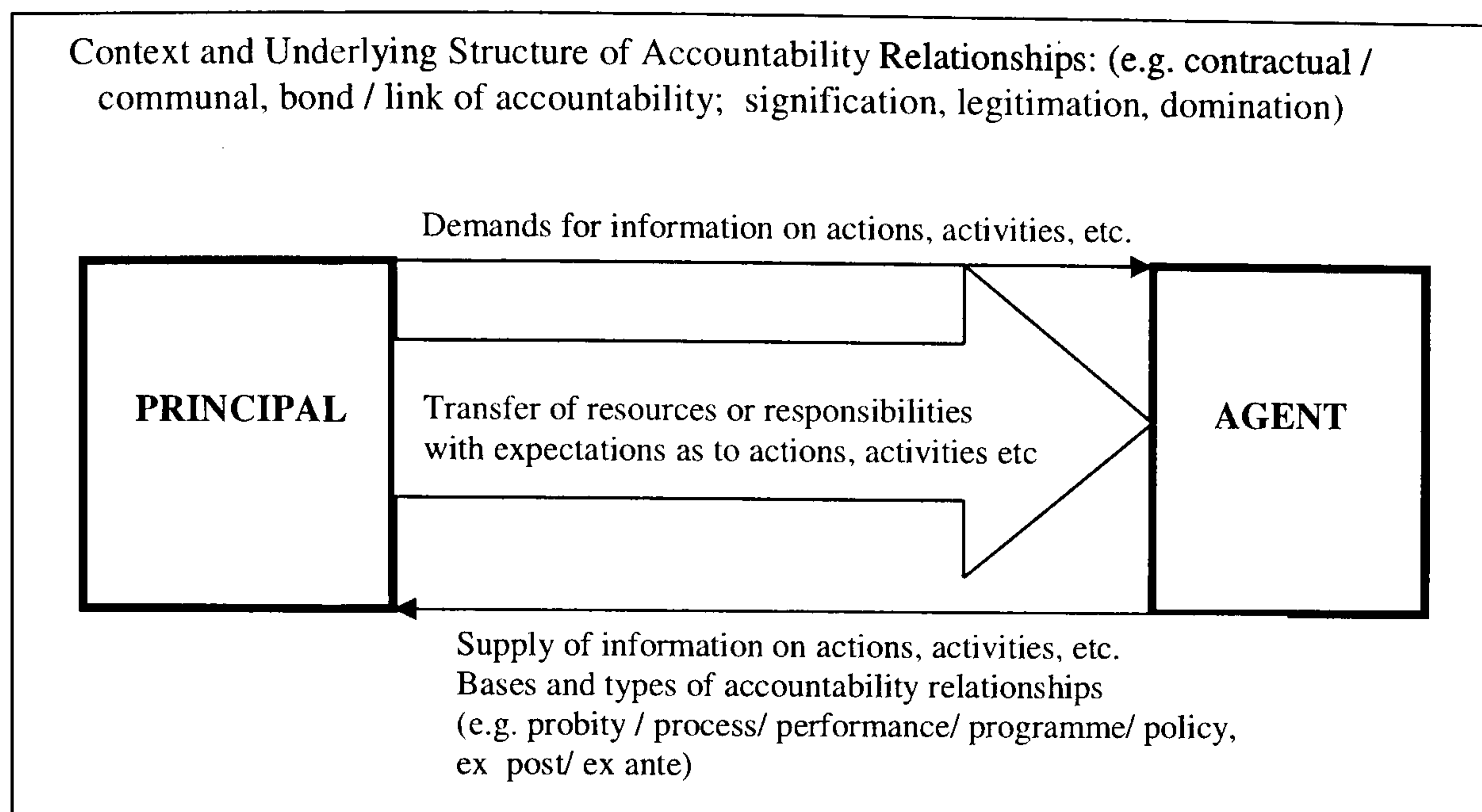


Fig: 2. 8: A summarised Picture of Theoretical insights (Laughlin, 1996: p 76)

Mayston (1993) reviews the significance of the principal agent model in the case of public sector organisations. According to him, the basic premise of the model is the perceived clash of interests between the principal and agent with respect to the utilisation of resources. The process of accountability aims to minimise the costs of agency to the principal. He, therefore, stresses that accountability is not an end in itself but a *means* to achieve another end which is *improvement in performance of the agent*. Using the principal-agent model, as a theoretical lens, has, therefore, an important consequence. Increasing accountability can only be justifiable if it leads to improved performance results. In economic terms, increasing accountability is only justifiable if the improvement in performance is greater than the costs of increasing accountability.<sup>28</sup> The limitations of the principal agent model in the context of complex public sector organisations are

<sup>28</sup> Mayston summarises the main themes of the theory. It is stated that three costs are important in the model. First *binding costs* which are incurred by the agent to assure the principal of his worthiness so that the principal doesn't use the powers of "incapacitation" or "deterrence". Second, the *monitoring costs* which are incurred by the principal to operationalise the act of taking accounts. Third, *residual costs* which result from agency relationships due to a clash of interest. Thus an increase in accountability can only be justified if it leads to a reduction in residual costs as against *monitoring* and *bonding costs* (ibid: 1993).



also discussed in the literature. For instance, a special issue of *Annals of Public and Cooperative Economics* considers usefulness of the principal agent model with respect to the UK regulated utilities, and all the authors from different disciplinary backgrounds identify important limitations to the model (Kassim and Price, 2005). This PhD research applies and adapts the basic principal agent model to the relationships of taxpayers, tax collectors and government.

Robinson (2003) takes a generic view of the system of accountability in a democratic state (i.e. Canada). He identifies *the public*, *provinces* and *federal government* as the main actors. The public provides tax money to provinces and federal government. The federal government transfers payments to the provinces. Thus both provinces and federal government are agents for the public which is acting as a principal. The public requires reports of performance and exercises its accountability powers through electoral process. Provinces also provide reports to the federal government for utilisation of the monetary resources provided by the federal government.

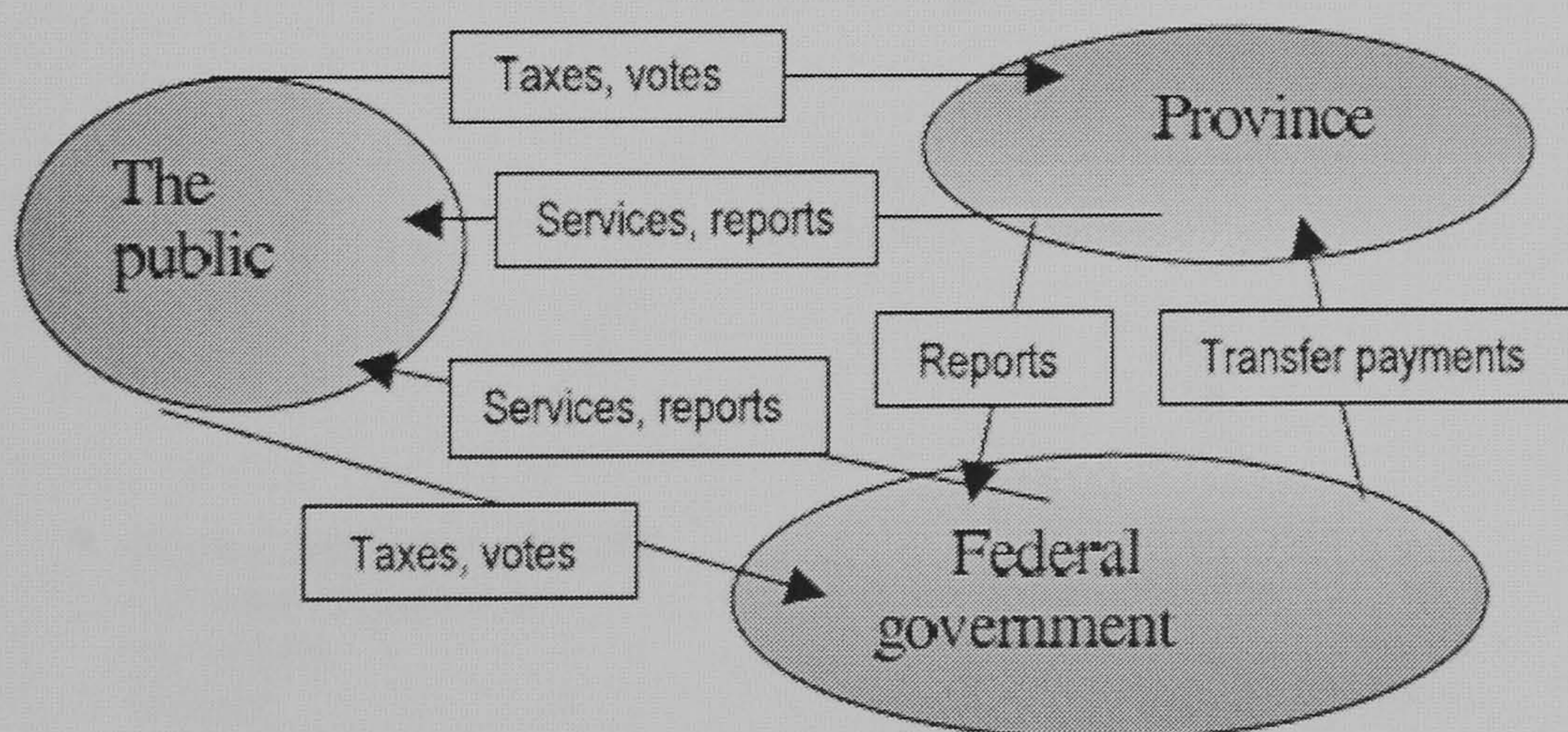


Fig 2.9: A simple model of accountability and performance reporting for Canadian government (Robinson, 2003: p 174)



Brignall and Modell (2000) draw insights from stakeholder theory and principal agent model to analyse organisational level accountability and PMS. They argue that the PMS of an organisation is shaped up by the pressures exerted by various internal and external stakeholders. They identify funding bodies and purchasers of services/products as the external stakeholders while the professional groups within the organisation as the internal stakeholders. Since for funding bodies, the main concern is how well the resources are utilised therefore they will be interested in using financial results and resource utilisation related performance measures as the basis of accountability. The purchasers’ pressures will emphasise quality, resource utilization and competitiveness as dimensions of performance while the professional groups will consider quality and innovation as the main dimensions of performance.

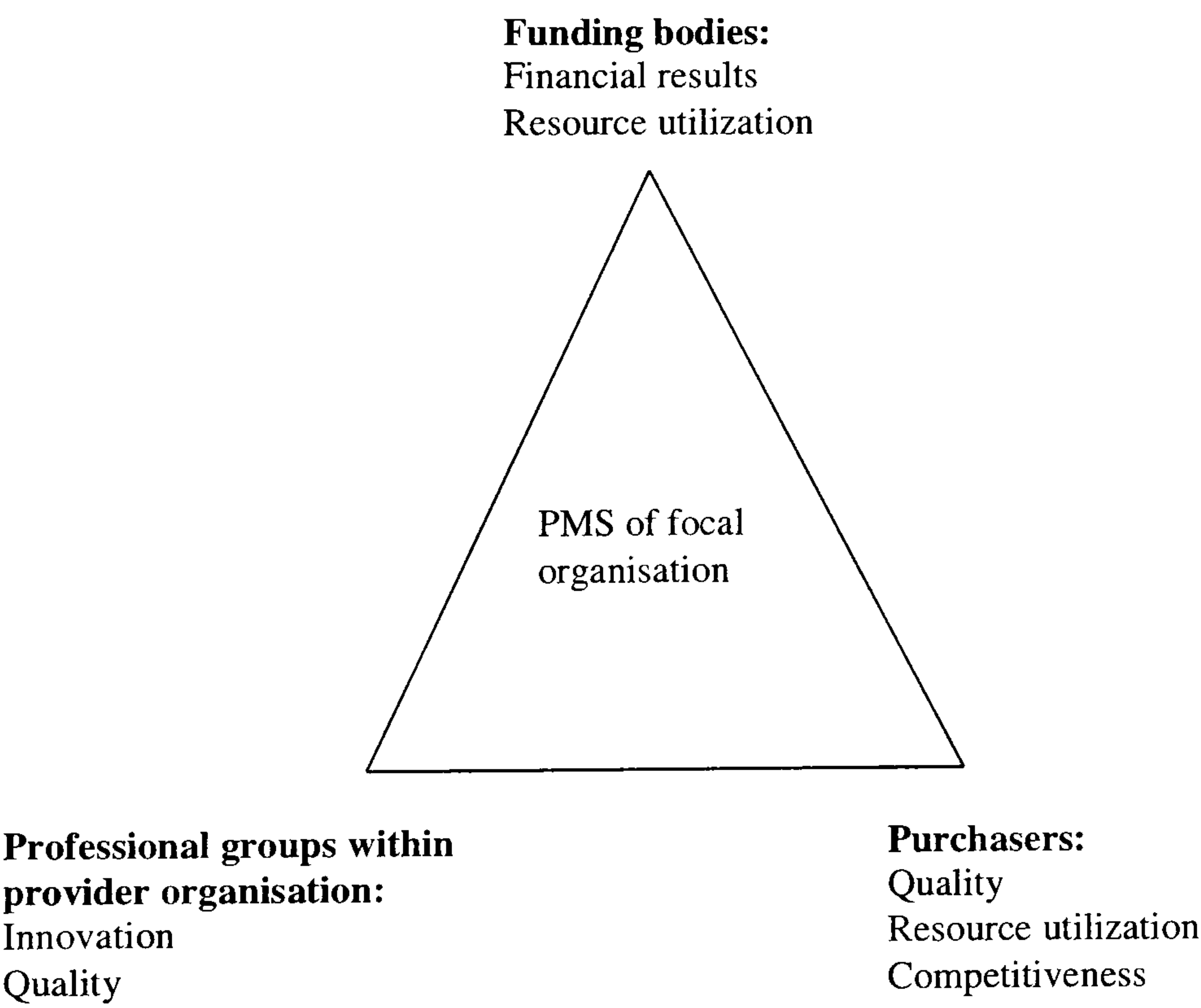


Fig 2.10: The influence of different stakeholder groups on the performance dimensions emphasised in the PMS of the focal organisation (Brignall and Modell, 2000: p 291)

From the preceding examples it emerges that some authors have tried to theorise the relationships between accounting, accountability relationships and stakeholders and present the insights with the help of simple models. Given the complexity of accountability relationships and PMSs such models do not explain the whole phenomenon. They however do highlight some important aspects of the accountability relationships.

Drawing inspiration from such models and using insights from stakeholder theory and performance measurement informed accountability literature, a simplified accountability model is proposed for the purpose of this PhD. The model will help in organising the analysis of the evidence and will be further developed as a result of insights drawn from this PhD study.

It was noted earlier that managers in a public sector organisation work under different types of accountability relationships. They have to respond to the expectations of different stakeholders through *public*, *managerial* and *legal* forms of accountability. The relationship under principal agent model requires that if the agent breaches the terms of agency relations the principal must have some powers to hold the agent accountable. Elster (1999: 255) provides a three-fold classification in this regard. If A is the agent of B, then in case of breach, B may dismiss A without punishing him further, punish him while retaining him as his agent, or dismiss him with additional punishment. The author terms the actual use of this remedial power by the principal as ‘incapacitation’. However when it is not actually used but the threat of its use in future remains then it is called ‘deterrence’. It is obvious that the principal, i.e. B, can exercise these two forms



of powers if he knows well whether the level of performance of A was up to his expectations or not? ‘Performance measurement’ can therefore be seen as a device which helps the principal use the powers of ‘incapacitation’ or ‘deterrence’ in an effective manner. It can therefore be concluded that performance measurement operationalises accountability relationships in any given organisation. When there are complex accountability relationships, it is important to examine the performance measures with a view to knowing as to which form of accountability relationship do these measures operationalise? These insights will be of primary importance when the PMS of HMCE is examined in the later chapters.

In order to develop a framework for analysing the multiple forms of accountability relationships and performance measurement in the public sector a simplified model of accountability relationships is proposed in the Fig 2.11

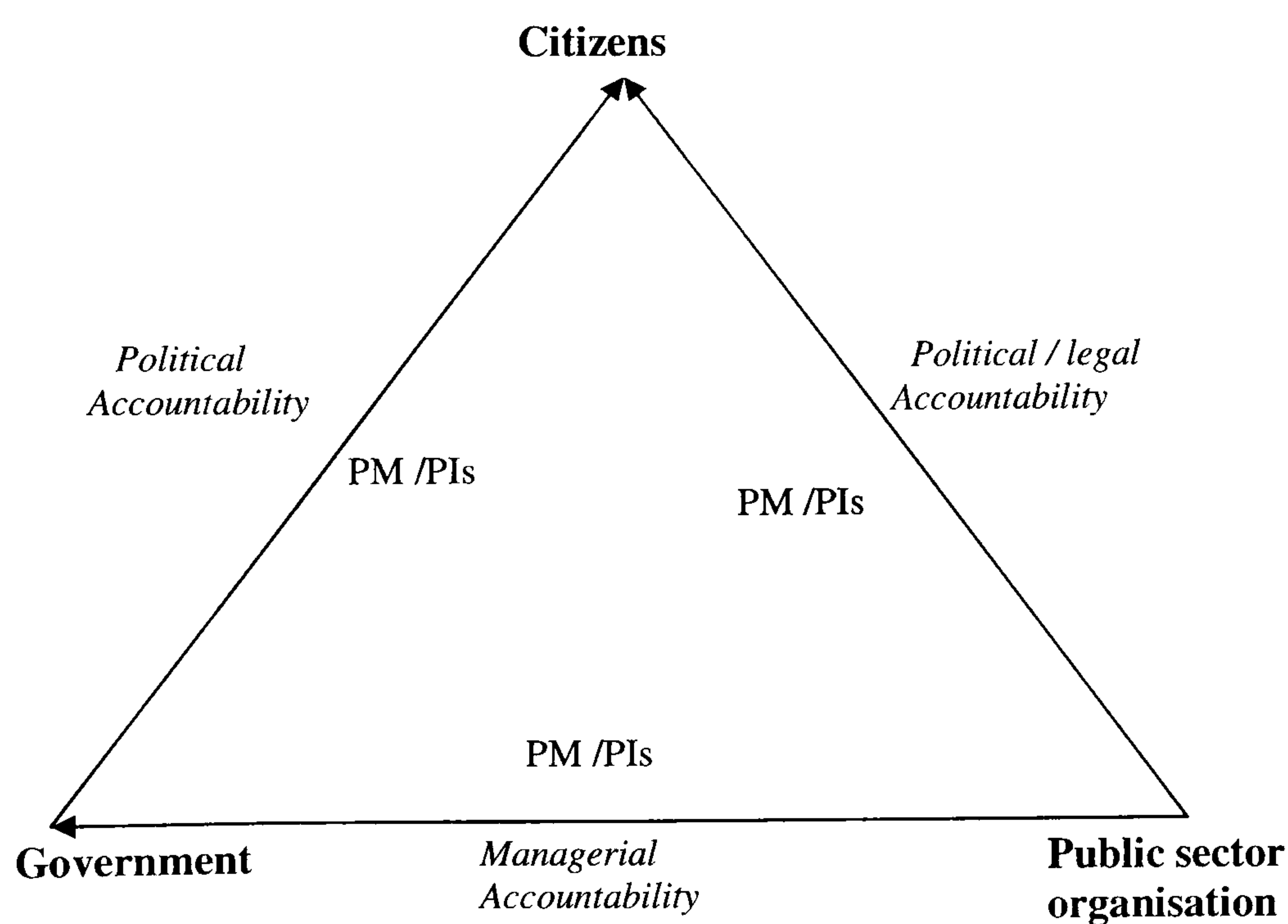


Fig: 2.11: A framework of multiple accountabilities in public sector management

Three main actors (or stakeholders) identified in this triangular relationship are *Government*, *Public sector organisations*, and *Citizens*. The arrows show the direction of accountability. The framework is built around the fact that a government provides services (and goods) to the citizens through public sector organisations which are the operational arms of the government.

*Managerial accountability* exists between the *Government* and a *public sector organisation*. It can be argued that through this accountability the central government exercises control over the public sector organisations with the help of performance measurement. This form of accountability is characterised by a formal PMS as the public sector organisation reports its performance against policy based quantitative targets on a regular basis.

The accountability relationship between the *Government* and *Citizens* can be termed as *Political* (or *Public*) as the *Government* is expected to fulfil the desires/demands of citizens who elected the government for that purpose. The government is therefore accountable to the citizens for performance on its election manifesto and other promises that it made with them. In the city states of ancient Greece, the government officials would render accounts of their performance directly to the gathering of citizens. But in the modern democracies this direct form of accountability is not possible as the citizens are too dispersed and heterogeneous to act as an effective principal<sup>29</sup>. The citizens in modern

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<sup>29</sup> Many authors view the efficacy of this public accountability with scepticism. For instance, Ferejohn (1999: 132) points out at least three serious limits to accountability within democratic institutions. First, the presence of electoral heterogeneity makes it possible for officials to play off some voters against others. Second, the officials have opportunities to avoid electoral responsibility for particular actions by grouping unpopular with popular actions. Third, the elected officials enjoy an immense informational advantage over voters in the wake of complexity of modern government. The author asserts that these three imposing impediments



democracies, therefore, allow parliamentary committees to do accountability of the government on their behalf. The quantitative and textual accounts of performance provided by the senior officials of governmental organisations are scrutinised by the parliamentary committees. The print and electronic media (e.g. T.V channels, newspapers, and journals) also help this accountability process by making the performance of the government and its officials more visible. In order to provide more credibility to this form of accountability, the parliament has deputed a few organisations specialising in the audit skills [e.g. National Audit Office (NAO)] to carry out audit of governmental departments.

*Citizens* are the recipients of the goods and services provided by the public sector organisations. The public sector organisations (like the Government itself) are accountable to the *Citizens*. The accountability relationship is of *political* and *legal* nature. The senior officials of public sector organisations are called to account by parliamentary committees, media and courts to explain their conduct. Here the performance measurement takes place through both textual and quantitative data as the senior management often uses both forms to highlight its achievements and defend against criticism.

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operate together to place a severe limitation on the possibility of a fully accountable democratic rule. In an empirical study involving change of governments due to economic performance, Cheibub and Przeworski (1999: 225-229) argue that “Rulers are accountable if the probability that they survive in office is sensitive to government performance; otherwise they are not accountable”. The study included all types of rulers like Presidents, Prime Ministers and aristocratic despots all over the world. The results of the study are termed as “surprising and dismaying” as the authors conclude that the survival of prime ministers is weakly sensitive to the growth of unemployment but the survival of presidents appears to be completely independent of economic performance.

The simplified framework has two important points to highlight. First, the public sector managers are under multiple accountability pressures. They have to provide performance reports sometimes directly for their own performance and sometimes they stand for the government. Second, consequently performance measurement of an organisation reflects such accountability demands. Since the accountability powers of all stakeholders are not equal (Brignall and Modell, 2000) the PMS of an organisation will contain mostly measures and indicators for that stakeholder which is able to exercise maximum pressure. Traditionally the resources provider is the most powerful stakeholder. Therefore if the public want to exert pressure upon the organisation, they have to adopt an influence strategy (Frooman, 1999). They will have to pressurise the resource provider to act on their behalf when placing accountability demands upon the organisation. Therefore, by examining the PMS of an organisation for a period of time, it is possible to analyse changes in multiple accountability relationships. The simplified framework will be used as an analytical tool to analyse the case of HMCE and will be further developed with the help of the evidence generated by this PhD case study.

## **2.5 Conclusion**

A review of the NPM based published literature establishes that enhancement of accountability with the help of PMS is one of the central issues. The debate on efficacy of multidimensional PMS in the public sector is inconclusive. The sceptics use NIS to question the claims made by the advocates of NPM in believing accounting to be a force of change. The rationalists on the other hand are



more interested in improving our understanding of performance measurement and accountability systems with the help of case studies. There is a growing emphasis that the institutional theory framework deserves more prominence in the accounting research. The need for conducting research in organisations having entirely new context is also well documented. No research has so far considered the issues specific to the performance measurement and accountability system of a tax administration. This PhD therefore fills the obvious gap in the literature. The published case studies on accountability systems have addressed the issue of enhancement of accountability or the tension between various forms of accountability relations. However there is no research which addresses the question as to how accounting changes mediate between competing accountability relations when two stakeholders demand and give accounts to each other on a reciprocal basis. The case of a tax administration provides an opportunity to address this gap in the literature.

The insights gained with the review of the literature in this chapter will be used to analyse the evidence relating to HMCE so that the less researched aspects of accountability in the public sector are highlighted.

## **Chapter 3**

### **Research Design and Methodology**

#### **Introduction**

A review of the published literature suggested that improving organisational performance with devices of accountability is one of the most important NPM inspired concerns. In the general management accounting literature the issue has been examined through various case studies (Ahrens and Chapman, 2002). It was noticeable in the literature review that the NPM has advocated the private sector practice of using performance measurement for enhancing accountability along with an increasing emphasis upon linking it more effectively to an organisation's overall strategic objectives. It was also noted that many scholars of the field (e.g. Collier, 2001; Broadbent, 1999; Broadbent and Guthrie, 1992; Hopwood, 1987, 83) have made calls for more case studies where the process of implementing accounting changes is critically examined. This PhD research aims to provide a rich description of such accounting changes in a completely new context, i.e. tax administration. In this chapter the methodology adopted by the PhD research with regards to gathering of evidence and analysis is explained.

#### **3.1 Importance of Research Area**

The need for case studies in the area of 'alternative research' was argued in the previous chapter. This PhD research focuses upon HMCE - a tax administration, which being a new contextual research site provides an opportunity for new insights into the process of implementation of accounting changes. The interest



in the field of tax management is inspired by the fact that tax authorities, despite their different context, have been required to adopt the NPM-inspired reforms in much the same way as other departments. However despite the importance of taxation matters in the overall functioning of business organisations, very little is published on tax administration issues in the mainstream journals. An empirical analysis of the data on published articles in academic journals was referred to in the previous chapter. Interestingly, no paper on performance measurement issues in the public sector is related to a tax administration.

It is this evident gap in the literature that prompted Tomkins et al. (2001) to express their concern over the fact that much public debate takes place about the calculation and incidence of different taxes but little academic research addresses the management problems that are specific to national taxation regimes.<sup>30</sup> The authors argue that tax authorities as public management sites are quite distinctive because of the interplay of so many different socio-political pressures emanating from external stakeholders.

The relative neglect of the tax authorities as research sites is all the more significant because these are also implementation locations of the NPM's "customer service" ideal where considerable re-conceptualisation of departmental aims and day-to-day services has occurred, arguably more than in other sites of NPM implementation (Hoskin et al., 2001). This is in contrast to many other public sector research sites like the NHS, local authorities, and the police which have received greater attention of researchers who have applied a

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<sup>30</sup> Lamb and Lymer (1999) also point out that research on taxation practice as it involves features of accounting – measurement, reporting, and analysis of financial performance – is under-researched.

variety of research methods ranging from extensive qualitative research (e.g. Collier, 2001; Broadbent and Laughlin, 1998) to analytical quantitative frameworks like data envelopment analysis and fuzzy set theory (e.g. Sun, 2002; Rangone, 1997). The call of Tomkins et al. (2001) has, however, failed to alter the research scene in a big way as the empirical survey revealed that during the last ten years only two articles have appeared in the academic journals which discussed managerial issues pertaining to HMCE. In view of the changes during last three to five years, the contents of those articles have little relevance now. It follows, then, that the absence of research on performance measurement in a huge and important public sector organisation like HMCE is potentially a significant gap in our understanding of public sector management, in general, and accountability through performance measurement, in particular.

The proposed PhD research, therefore, aims to investigate the ways in which PMS works as a tool of enforcing, enhancing or modifying accountability relationships in HMCE. The central research question which guides the course of PhD research is:

*How are accountability relationships defined and operationalised with the help of performance measurement in the case of a tax administration and to what degree NPM inspired accounting changes alter such relationships?*



3.2 Ontological and Epistemological Foundations

Burrell and Morgan (1979) popularized the oft-quoted framework of four juxtaposed paradigms<sup>31</sup> within the social theory.

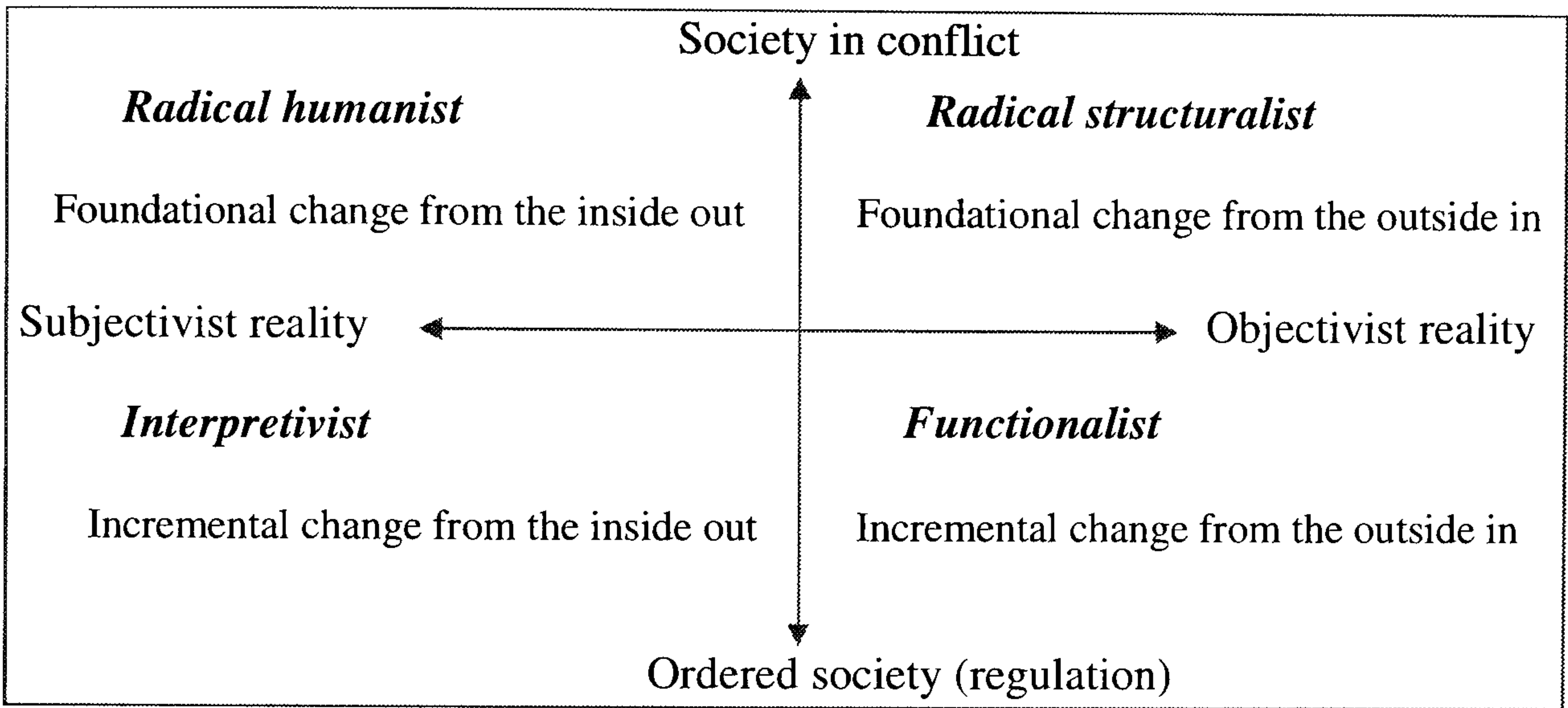


Fig 3.1: Four paradigms of social science research (Burrell and Morgan, 1979: 25)

The matrix is based on four main debates in sociology:

- is reality given or a product of the mind?
- must one experience something to understand it?
- do humans have "free will", or are they determined by their environment?

<sup>31</sup> The authors identify four paradigms represented by the quadrants of the matrix. First, the ‘Functionalist Paradigm’ (objective-regulation) has remained the dominant paradigm for organisational study. Assuming rational human action it shares a belief that one can understand organisational behaviour through hypothesis testing. Second, ‘Interpretive Paradigm’ (subjective-regulation) explains the stability of behaviour from the individual's viewpoint. Third, ‘Radical Humanist’ Paradigm (subjective-radical change) is mainly concerned with releasing social constraints that limit human potential. They see the current dominant ideologies as separating people from their "true selves". They use this paradigm to justify desire for revolutionary change. And lastly ‘Radical Structuralist’ Paradigm (objective-radical change) sees inherent structural conflicts within society that generate constant change through political and economic crises. This has been the fundamental paradigm of Marxists.

- is understanding best achieved through the scientific method or through direct experience?

The authors encapsulate the aforementioned debates into two fundamental issues that form the axes of the *two by two* matrix:

- social theories emphasizing regulation and stability as against those which advocate radical change
- theories built upon subjectivity (individualistic) as against theories based on objectivity (structural)

Referring to the approving silence after the publication of Burrell and Morgan's (1979) book on paradigms, Willmott (1993: 691) argues that it escaped critical examination, perhaps because it could pass as a textbook rather than as a distinctive and highly influential contribution to the development of its field. Admitting that the publication reflected and reinforced a growing disaffection with the dominant, functionalist orthodoxy, the author calls for breaking the dogma because if the claimed division of paradigms is taken seriously, it would unnecessarily constrain the process of theory development within polarized sets of assumptions about science and society. This PhD researcher follows the advice and, therefore, the ontological and epistemological foundations of the PhD research are influenced by the insights drawn from *Critical Realism* and Laughlin's (1995) '*middle-range*' thinking.

Authors (e.g. Mingers, 2000; Bhaskar, 1998) advocating *Critical Realism* as the basis of social research argue that social structures do not exist independently of the activities they govern. Social structures are thought not to be universal but



localised in both space and time. On the epistemological side, the possibilities of measurement are thought to be limited since intrinsically the phenomena are meaningful and meanings can not properly be measured and compared but only understood and described.

Laughlin (1995: 64) states that 1980s generated a wide range of empirical studies in accounting from various theoretical and methodological approaches which resulted in increased tension in the literature between different proponents of various approaches. Referring to Burrell and Morgan's schema of paradigms he argues for a simpler classification based in terms of choices ranging from low to maximum made on three dimensions of *theory*, *methodology*, and *change* as shown in Fig 3.2. Laughlin advocates 'middle range' thinking, wherein the conceptual models are always "skeletal" requiring empirical "fleshing out". According to Laughlin, these empirical insights do not necessarily attempt to test a theory but rather aim to amplify and refine it. It is further argued that with current levels of understanding, it is impossible to use the models either to predict exactly how the organisational arrangements will look in specific instances or which pathway will be followed from any actual disturbance. The author, therefore, advocates "middle range" (Fig 3.2) as all theories continually require amplification and refinement through empirical examples.

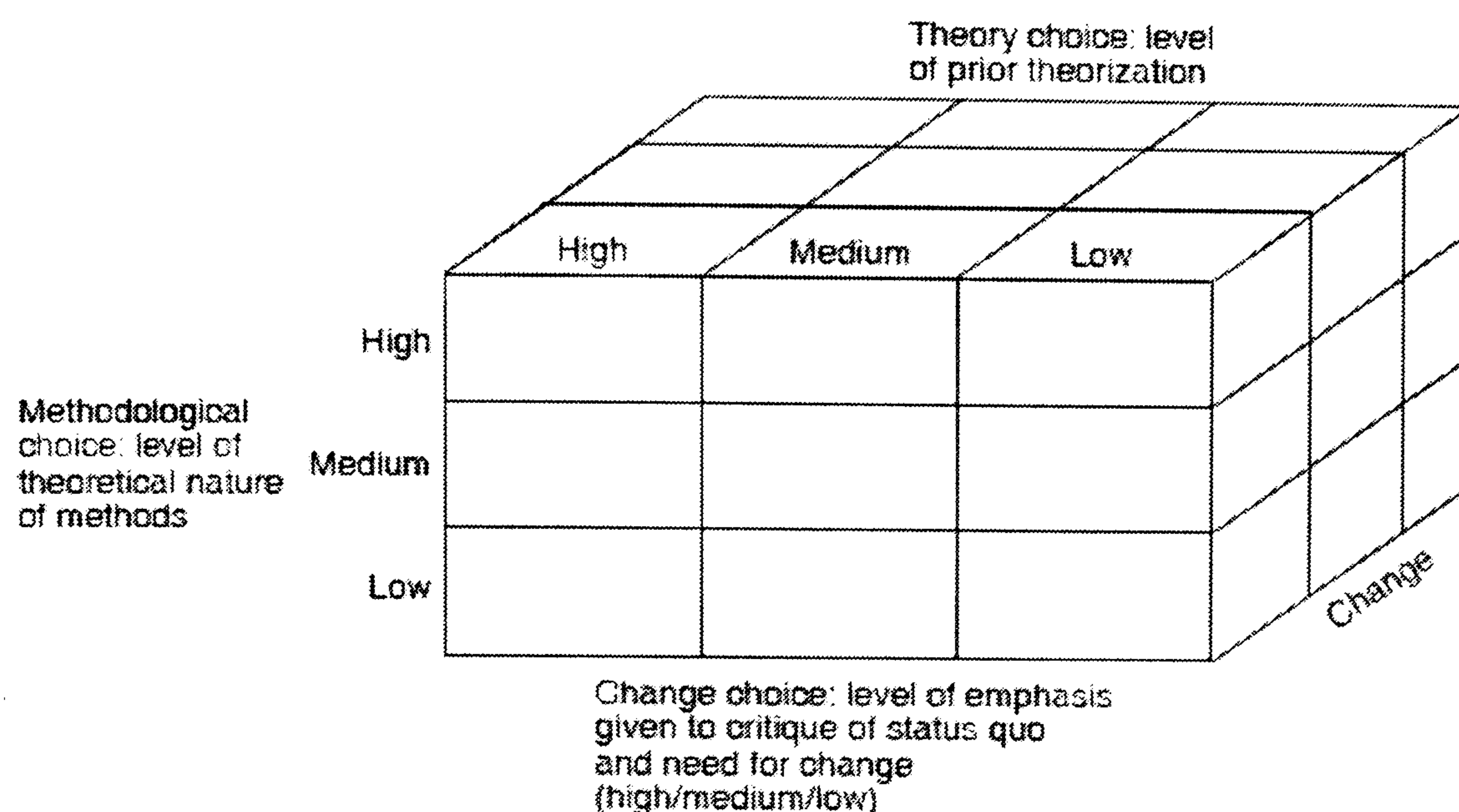


Fig 3.2: Choices under Middle Range Thinking (Laughlin, 1995: p 68)

The PhD research followed this advice of Laughlin by proposing a skeletal framework of accountability with the help of stakeholder and institutional theories informed principal-agent framework of accountability. The framework is then fleshed out by the evidence collected from the research.

### 3.3 Research Approach

The PhD research adopted the case study approach as it desired to study the accountability for performance in HMCE in its bounded context. A case study is often associated with qualitative research however it maybe based upon quantitative techniques as well. According to Denzin and Lincoln (1994: 2), qualitative research is multi-method in its focus, involving an interpretive, naturalistic approach to its subject matter. They argue that the qualitative researchers study things in their natural settings in order to make sense of phenomena in terms of the meanings people bring to them. Merriam (1985: 4) characterises qualitative research as an umbrella concept covering several forms



of inquiry that help to explain the meaning of social phenomena with as little disruption of the natural setting as possible, and in which the focus of the study is on interpretation and meaning. Padget (1998) has tabulated the differences between qualitative and quantitative forms of research.<sup>32</sup>

Qualitative	Quantitative
Inductive	Deductive
Naturalistic; in vivo	Scientific Method Decontextualising
Uncontrolled Conditions	Controlled Conditions
Open Systems	Closed Systems
Holistic; Thick Description	Particularistic
Dynamic Reality	Stable Reality
Researcher as Instrument of Data Collection	Standardised Data Collection Instruments
Categories result from Data Analysis	Categories Precede Data Analysis

Table 3.1: Distinctions between Qualitative and Quantitative Research:  
(Source Padget, 1998: p 14)

**3.4 Case Study as a Research Method**

The importance of research methods in production of knowledge can not be over emphasised (Pinsonneault and Kraemer, 1993)<sup>33</sup>. As the name suggests, a *case* or *cases* are studied in case study form of research. Stake (1995) calls the ‘case’ an “integrated system”, Smith (1978) uses the term “bounded system”, and Miles and Huberman (1994) refer to the case as “a phenomenon of some sort occurring in a bounded context”. Despite the popularity of case study as a research method, defining case study is not always so simple. For instance, Lincoln and Guba (1985) state:

<sup>32</sup> It is argued that qualitative research is often concerned with a reality that is dynamic and hard to be understood fully with mere numerical analysis based on questionnaires. The researcher collects data by becoming a part of the environment that is studied. Thus theory is therefore induced in the case of qualitative research unlike quantitative research which is based on deductive method.

<sup>33</sup> Benbasat and Weber (1996, p. 392) state that "*Research methods shape the language we use to describe the world, and language shapes how we think about the world*".

“While the literature is replete with references to case studies and with examples of case study reports, there seems to be little agreement about what a case study is.” (p.360)

Yin (1984: 23) in his definition of a *case study* identifies three important qualifications as he terms it as an empirical inquiry that:

- (a) investigates a *contemporary* phenomenon within its real-life *context*; when
- (b) the *boundaries* between the phenomenon and context are not clearly evident; and in which
- (c) *multiple* sources of evidence are used.

Yin (1994: 9) suggests that a choice between case studies and other empirical methods might be rationally made against three conditions:

- (a) *type* of research question being posed; (If the question is of exploratory nature which desires to study a phenomenon in detail then case study is the desirable choice)
- (b) extent of *control* a researcher has over actual *behavioural* events; (If there is little control then case study is the favourable choice)
- (c) degree of focus on *contemporary* as opposed to historical events; (For studying contemporary phenomenon in detail case study method is a desirable research method)

### **3.5 Appraising Case Study as a Research Method**

Yin (1989) compares strengths and alleged shortcomings of case study method. The most important advantage of case study research is stated to be its ability to provide rich understanding of reality by laying emphasis upon detailed contextual analysis. The alleged weaknesses are enlisted as lack of rigour, sloppy



investigation and equivocal evidence. It is also alleged that bias is more frequently encountered and less frequently overcome in case study method. Becker (1991) suggests that researchers may have "feelings" for the subjects and that conclusions that are drawn suffer from a lack of reliability. Oversimplification or exaggeration of a situation is another possible weakness leading the reader to distorted or erroneous conclusions about the actual state of affairs (Guba and Lincoln, 1981). Labour-intensiveness of the method also makes it less popular with many researchers. Lack of generalization and lack of rigour (Yin, 1989; Guba and Lincoln, 1981) are two most important alleged shortcomings of case study research method. Therefore both are briefly discussed next.

#### **i. Generalising from Case Studies**

Some authors (e.g. Eisenhardt, 1989) have tried to defend the power of case study in theory building. Others like Lincoln and Guba (1985) are less apologetic and responding to the issue of generalisability argue that since every human organisation is context specific therefore no generalisable laws can ever be effectively deduced.

Stake (1978: 5) describes the generalisability of case studies as 'naturalistic', that is, context-specific and in harmony with a reader's experience, and thus 'a natural basis for generalization'. This means that case study findings often resonate experientially or phenomenologically with a broad cross section of readers and thus facilitate greater understanding of the phenomenon in question.

Jensen and Rodgers (2001) argue that a *case study* desires to question generalization to a larger population by focusing on a single entity. Keating (1995: 68) refers to the definition of theory by Sutherland (1975) as “an ordered set of assertions about a generic behaviour or structure assumed to hold throughout a significant range of specific instances”. Keating claims that a case study can make significant contribution towards theory development. They identify three stages of the process of theory development where a case study can make such contribution. Those are *theory discovery*, *theory refinement*, and *theory refutation*. The authors argue that these three stages provide relatively natural categories for classifying case study research and researchers usually focus their attention on one of the three stages, although some case studies span more than one stage of development (p 84).

According to Stake (1995), previously unknown relationships and variables can emerge from case studies and lead to a rethinking of the phenomenon. He contends that the knowledge learned from case study is more concrete and contextual, resonating with the reader's experience because it is more vivid and sensory than abstract.

Yin (1989, 1993) proposes developing formal explanatory propositions (including rival propositions) to be tested via data collection and analysis against criteria relevant to their acceptance or rejection. On the other hand Eisenhardt (1989) argues that *a priori* formal propositions can inhibit exploration of the cases and development of novel propositions, and supports the development of tentative theoretical constructs to inform the study, and an iterative process that links data to the emerging theory.



In this PhD research both Laughlin (1995) and Eisenhardt (1989)'s advice has been followed with regards to use of *a priori* specification of theoretical propositions. While insights were drawn from stakeholder, principal agent and institutional theories, the empirical evidence was collected and analysed without any stringent attachment to any single theoretical framework. Following Jensen and Rodgers (2001), this PhD research selected a single case study because a tax administration has contextual features of its own and needs to be studied in its entirety. The case study is expected to make its contribution towards theory refinement (Keating, 1995), as it will improve our understanding of the process of implementing accounting changes and modification of accountability relationships.

## **ii. Lack of Rigour**

In order to overcome this objection on case study research some authors propose the use of combined or multiple methods, e.g. triangulation techniques. Denzin (1984) identifies four types of triangulation:

- data source triangulation, when the researcher looks for the data to remain the same in different contexts;
- investigator triangulation, when several investigators examine the same phenomenon;
- theory triangulation, when investigators with different viewpoints interpret the same results; and
- methodological triangulation, when one approach is followed by another, to increase confidence in the interpretation.

By using a combination of observations, interviewing, and document analysis, the fieldworker is able to use different data sources to validate and cross-check findings (Patton, 1990). In order to ensure rigour this PhD research also paid attention to the need of triangulation. The textual data was, therefore, acquired from different sources which were entirely independent of each other. The interviewees were also selected from two different regions and belonged to various levels of seniority in the organisation. In this way data triangulation was achieved in terms of Patton (1990)'s definition. Different theoretical frameworks (e.g. social exchange theory, NIS, Results and Determinants Framework) were applied to the research evidence which therefore resulted in achieving theoretical triangulation as well.

The research question of this PhD study meets the qualifications cited by Yin (1989) with regards to a choice between case studies and other empirical methods. Since HMCE is a central government department where culture of secrecy is well documented (Gillman, 1987: p 8), permission for a questionnaire-based survey would have been impossible without compromising the researcher's independent and critical analysis. Moreover, accountability is an abstract notion, and customer focus related notions are not well developed in the case of a tax administration, therefore, in-depth interviews helped in constructing reality which would not have been possible with simple survey based research. Therefore, the case study method based on qualitative data was the most appropriate research method for this PhD research.



### **3.6 Case Study Research and Management Accounting**

In the accounting discipline, the case study method has won widespread support after calls were made for more qualitative research in accounting. For instance, Otley and Berry (1994) support the use of case study approach in accounting by claiming that case study research is a vehicle by which theories can be generated and modified in the light of data. They believe that the case study method provides a more holistic approach where existing theories are inadequate or incomplete, or explain only a subset of the phenomenon of interest.

With a view to finding guidance from the earlier published research in the relevant research fields of accounting, the articles published in various journals were reviewed by this PhD researcher and it was found that the methods used were quite diverse. The research methods depended both upon the scope of the research and the nature of the researched entity. However the use of qualitative research methods like semi- structured interviews was found to be a recurrent feature. For instance, Malmi (2001) in a study on balanced scorecard usage adopted the method of semi-structured interviews, terming it ‘the most suitable method’ for that kind of study. Similarly, Kloot and Martin (2000) investigated strategic performance management in local government by using a qualitative methodology of interviewing councillors, the CEO, executive directors and managers of Victorian local government. In an earlier reported research, Kloot (1999) also adopted the semi-structured interviews method to examine performance measurement practices in 23 of Victoria's 78 local governments. The researcher contends that field studies and interviews provide richer data than can be gained from survey research, and can explore causal effects.

Moon and Fitzgerald (1996) studied the characteristics of the PMS of a courier company; TNT. They used semi-structured interviews together with an examination of internal documents and non-participatory observation of company practices, including company meetings. In somewhat similar research, Brigham and Fitzgerald (2001) carried out a detailed, in-depth case study of a large UK water company, which provides clean water and sewerage services. They used semi-structured interviews and documentary sources in the public domain for gathering textual data. Broadbent and Laughlin (1998) conducted semi-structured interviews of teachers and head teachers in 24 schools and staff of 34 GP practices for an analysis of their coping strategies in the wake of performance reporting changes.

Otley and Berry (1994) review the role of case study methods in management accounting research by referring to four published case studies on management accounting and organisational control. Despite different methodological stances by the researchers in the different studies, there was a striking similarity in the methods of data collection adopted. These included documentary evidence concerning formal control systems, design and use; semi-structured interviews with managers, generally at levels both above and below the level of central interest; the observations of meetings wherever possible; and collection of information on the external context in which the company operated.

Many case studies have considered the impact of NPM upon various public sector organisations. For instance, Christensen and Yoshimi (2001) use NPM as a framework for their analysis of performance reporting regimes of Australia and



Japan.<sup>34</sup> Modell (2001) studies the NPM inspired performance measurement reforms of the public health care sector in Norway from an NIS perspective by examining the responses of senior management and staff. Robinson (2003) examines the adoption of performance measurement as a tool of accountability by the Alberta government to highlight the unintended consequences of the use of scientific managerialist techniques in the public sector. Kurunmaki et al. (2003) carry out a comparative study of management accounting changes in intensive care units in the UK and Finland where they draw upon the institutional theory. Collier (2001) describes the introduction of management accounting change in the form of local financial management in a police force using an ethnographic study.

In view of the preceding merits of case study research, the PhD research was based upon a carefully designed case study of HMCE which is discussed in the next section.

### **3.7 Research Design**

Emphasis upon good research design for a case study research is well documented (e.g. Stake, 1995; Yin, 1989). It is argued by Goetz and Lecompte, (1984: 228) that while survey based researchers hope to find data to validate a theory; it is often a case with qualitative researchers that they hope to find a

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<sup>34</sup> Using Hood (1995)'s articulation of NPM as a set of 7 doctrines, the authors observe that the doctrine no 6 of using performance measurement as a managerial tool is of central importance to NPM framework. The authors claim that the primacy of accounting in NPM has received attention in the literature leading to improved terminology resulting in the phrase 'new public financial management' (NPFM):

“development of a performance measurement approach, including techniques such as financial and non-financial performance indicators, league tables, citizen's charters and program evaluations” (Olson et al. 1998, p 18)

theory that might help explain their data by inductive methods. However, no research can advance in a complete theoretical vacuum. Yin (1993) advocates a more positivist model of case study. His requirements for formulating a case study are the capability to deal with a diversity of evidence, the ability to articulate research questions and theoretical propositions, and the production of a research design. He advises use of triangulation for greater reliability and validity. Laughlin (1995) also advocates some skeletal theorising before the start of research so that the data analysis contributes to the process of theory development. In the formulation of this PhD research design the advice of both Laughlin and Yin was followed. The essential ingredients of a good case study research as proposed by Yin (1989) are discussed next with regards to this PhD research.

#### **i. Research Questions**

As stated earlier, this PhD research is guided by the following main research question:

*How are accountability relationships defined and operationalised with the help of performance measurement in the case of a tax administration and to what degree NPM inspired accounting changes alter such relationships?*

It was established in an earlier section that there is not a single paper published in the academic journals on accountability through performance measurement in the case of a tax administration. The non-academic sources such as annual reports of the organisation do provide information on organisational activities. But limitations of such reports in providing a satisfactory answer are obvious as Phillips and Hardy (2002) argue that in a discourse analysis a researcher does not simply focus on an individual text but rather refers to bodies of texts because it is



the interrelations between texts, changes in texts, new textual forms, and new systems of distributing texts that constitute a discourse over time.

Since accountability in terms of a process can be defined as *giving* and *taking* of *accounts*, four elements can be identified in the process of accountability with reference to the principal-agent model:

- The Principal who provides resources and who demands accounts
- The Agent who controls the resources and provides accounts
- The Accounts
- Remedial powers

(adapted from Sherer and Kent, 1983)

Applying this identification to the research question the following constituent elements become important:

1. Who is (are) the principal (principals) in the case of a tax administration?
2. Who is (are) the Agent (agents) in the case of a tax administration?
3. What is the format of accounts and what are its contents for the purpose of performance measurement and reporting?
4. What are the remedial/control powers available to the principals?

These questions helped in organising analysis of the evidence regarding official attempts at using accounting changes for modifying accountability relationships.

In addition to the preceding questions, the following set of questions suggested by Otley (1999) for defining performance management of an organisation was also used for guidance.

1. What are the key objectives that are central to the organisation's overall future success, and how does it go about evaluating its achievement for each of these objectives?
2. What strategies and plans has the organisation adopted and what are the processes and activities that it has decided will be required for it to successfully implement these? How does it assess and measure the performance of these activities?
3. What level of performance does the organisation need to achieve in each of the areas defined in the above two questions, and how does it go about setting appropriate performance targets for them?
4. What rewards will managers and other employees gain by achieving these performance targets or, conversely, what penalties will they suffer by failing to achieve them?
5. What are the information flows feedback and feed-forward loops that are necessary to enable the organisation to learn from its experience, and to adapt its current behaviour in the light of that experience?

When performance measurement is used strategically, it is always a part of the overall performance management system of an organisation, as can be seen from Otley's (1999) framework. While the emphasis of this PhD study is on performance measurement of HMCE, it benefited by remaining attentive to Otley's framework. The insights drawn from stakeholder theory, private sector performance measurement frameworks and institutional theory were also used to critically examine the evidence collected by the PhD evidence.



#### **iv. Research Design**

A good research design is an essential element of a case study research as suggested by Yin (1989). This PhD research was designed after a careful consideration of both research requirements and ground realities. Being a PhD research project, the monetary constraints were considerable. The research concerned a central government department with approximately 22000 employees in a wide variety of work patterns as explained in Chapter 4. The primary data was therefore collected by focusing upon VAT administration of the department as it not only represents almost 60% of the total tax collection of HMCE but also employs the highest proportion of employees. Face-to-face in-depth interviews were held with middle and operational-level employees where the discussion centred on the notion of accountability for performance. The purpose of interviewing employees at different levels of responsibility was to find evidence of the effects of implementing accounting changes. The basic premise was that if the changes were successful, the effect would be noticeable in the discourse of the personnel of HMCE. Another purpose of these interviews was to array the notions of performance measurement in the employees discourse against the officially described notions and practices.

Since the top management of a government department is not normally expected to deviate from the official policy guidelines, an innovative use of parliamentary committee reports was employed by this PhD research. In these select committee hearings the senior managers of government departments are obliged to answer all sorts of probing questions.

An interview instrument (Annex 3.1) was designed which helped to keep a focus upon main research question during the interviewing sessions. The semi-structured extensive interviews were tape recorded with the permission of the interviewees, however anonymity was guaranteed. Therefore alphanumeric symbols have been used instead of their names and rankings. The interviews were later transcribed and page numbered. All the letters, emails and documents received from the department during the course of research were also numbered and titled in the same way (Annex 3.2).

Miles and Huberman (1994) stress that textual data analysis should follow a structured pattern so that reliability of the conclusions drawn is robust. They suggest that the data analysis should be done in a structured manner, such as ‘first-level’ coding, ‘pattern’ coding and ‘memoing’. The authors define *codes* as ‘tags’ or ‘labels’ for assigning units of meaning to the descriptive or inferential information<sup>35</sup> compiled during a study. The first-level coding involves reviewing the transcripts ‘to dissect them meaningfully while keeping the relations between the parts intact....’ (ibid: 56).

This PhD author used underlining and colour highlighting of the interview transcripts, archival documents and parliamentary source material to do first order coding.

Miles and Huberman (1994) state that after initial coding, the textual data may be

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<sup>35</sup> These can be attached to “chunks” of varying size – words, phrases, sentences, or whole paragraphs, connected or unconnected to a specific setting.



pulled together into categories. According to the authors, this ‘pattern coding’ is a way of grouping those summaries into a smaller number of sets, themes, or constructs’ ( p. 69). They further suggest that the pattern coding be followed by ‘memoing’ to help in organising the themes and categories which should lead towards more general concepts<sup>36</sup>. Following Miles and Huberman (1994), this PhD author also used ‘pattern coding’ by making categories and sub-categories of codes assigned to the textual data. The emerging discourse was then critically analysed for obtaining answers to the research questions.

### **iii. Diversity of Evidence**

Textual data for the purpose of analysis was acquired from diverse sources. Each source on its own would have been insufficient in providing satisfactory answers to the research questions however when they are interrelated, it was possible to generate a discourse providing more credible answers. The following sources formed the basis of analysis:

#### **1. Primary Sources**

##### **a. Preliminary Interviews with Tax Advisors/Tax Researchers**

Three university academics well known for their research in the field of tax administration were interviewed at the very outset of the research in mid 2002.

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<sup>36</sup> According to Miles & Huberman, (1994, p. 72) ‘memoing’ refers to the theorising write-up of ideas about codes and their relationships as they strike the analyst while coding.... It can be a sentence, a paragraph or a few pages ... they tie together different pieces of data into a recognisable cluster, often show that those data are instances of a general concept.... It is one of the most useful and powerful sense-making tools at hand.

Two tax practitioners were also interviewed one of whom represented the VAT practitioners group in early 2003. Twenty written replies were obtained on questions pertaining to perception of HMCE among the tax practitioners in late 2004. The purpose of interviewing tax advisors and obtaining written replies was to acquire insights into the perceptions held by those who interact most with the tax officials.

**b. Conferences**

Two conferences where HMCE made official presentations were also attended by the researcher at an early stage of the research in 2002 to gain extra opportunity of observation and data gathering.

**c. Interviews with Personnel of HMCE**

Twenty semi-structured in-depth interviews were conducted with the personnel of HMCE in small intervals in 2003. The number of interviews was not extended because an analysis of the twenty interviews transcripts revealed considerable core evidence. The interviewees represented various levels, places and work patterns. Two belonged to senior management level, five to HQs, seven to middle level regional management and six to the field/operational level. Five others dealing with performance related issues corresponded through posts and emails.



## **2. Secondary Sources**

### **d. Annual and Spring Reports**

The reports contained useful information on departmental activities and results of those activities. By employing a longitudinal analysis of the reports during 1997-2003, significant insights were gained regarding organisational and accounting changes in the organisation.

### **e. Departmental Strategy Papers and Other Reports**

High level policy papers of the department provided insights into the strategic level thinking of the organisation. Many other special reports also provided useful information on areas of importance to the organisation (Annex 3.3).

### **f. Policy Papers of Central Government**

The policy papers of the central government helped in understanding the external context of the performance measurement of HMCE and related issues (Annex 3.4).

### **g. Tax Administration Policy Papers of OECD**

The policy papers issued by OECD also helped in further understanding of external environment, and practices in many other tax authorities.

#### **h. Reports/Evidences before Parliamentary Select Committees**

The senior management of HMCE, like all other departments, presents oral and written evidence before the parliamentary committees, especially, Treasury Select Committee (TSC). Since the managers are interrogated intensely by the members of the committee, the data source was important for gaining access to the views of the top management of HMCE on important organisational matters.

### **3.8 Conclusion**

It was noted in Chapter 2 that rationalist and sceptic writers (termed ‘alternative research’ by Broadbent and Guthrie, 1992) consider ‘context’ of an organisation very important. Since HMCE was an organisation with a historical tradition of veiling itself in a cloak of secrecy, interviews with HMCE personnel and a review of its internal and external documents helped in understanding the context of this organisation. The primary textual data also helped in investigating the effect of accounting changes implemented by HMCE during the period of analysis. By analysing the textual data obtained from diverse sources (interviews, official publications and documents, parliamentary committees reports) and the course of events the aim is to answer the research question. In the next chapter the organisation is explained in detail so that the ‘veil’ on HMCE gets raised somewhat and its context can be understood for the purpose of analysis of evidence in the later chapters.



## **Chapter 4**

### **Her Majesty's Customs and Excise– an Overview**

#### **Introduction**

In this chapter the department of HMCE (HMCE) is introduced. The historical origins of the department are also discussed in detail so that the ethos of the organisation can be clearly understood. This understanding will be of primary importance when the accountability system and nature of accounting changes are analysed in the subsequent chapters.

#### **4.1 The Department**

The HMCE is a central government department. In the official Annual Report, 2002 HMCE is described as the department which is responsible for “collecting indirect taxes and enforcing Government requirements relating to the movement of goods into and out of the UK.”, and whose job is “managing certain major risks on behalf of the Government and the public (HMCE, 2001a: p7). This deceptively simple portrayal of the department fails to bring forth the heterogeneity and complexity associated with the functions performed by the department. The official publications of the department are not without references to this ironic misperception:

“Most people know us as the uniformed officers who check your bags at ports and airports, or as “The VAT Man” but we do a lot more than this” (HMCE, 2002a).

It can be argued that the difficulty in understanding the true profile of the department is attributable to two main reasons. First, unlike majority of other public sector departments, HMCE has largely remained a closed organisation, having kept itself at a distance from the prying eyes of external analysts and researchers.

“The Customs and Excise are one of Britain’s longest-established institutions, with their activities recorded in Magna Carta . . . They are also one of the more closed bodies of British society, whose inner workings are only rarely exposed to the glare of publicity, if at all” (Gillman, 1987: p 8).

In addition to this self-professed isolationism of the department, the second reason is the highly technical and professional nature of the work performed by the employees of the department which often acts as an enormous barrier for the external analysts and researchers. No wonder one comes across very little academic work on the various managerial issues confronted by HMCE.

The HMCE is primarily concerned with collection of indirect taxes and enforcement of anti-smuggling laws, as is evident from the following pronouncement which appears on the official website of the department:

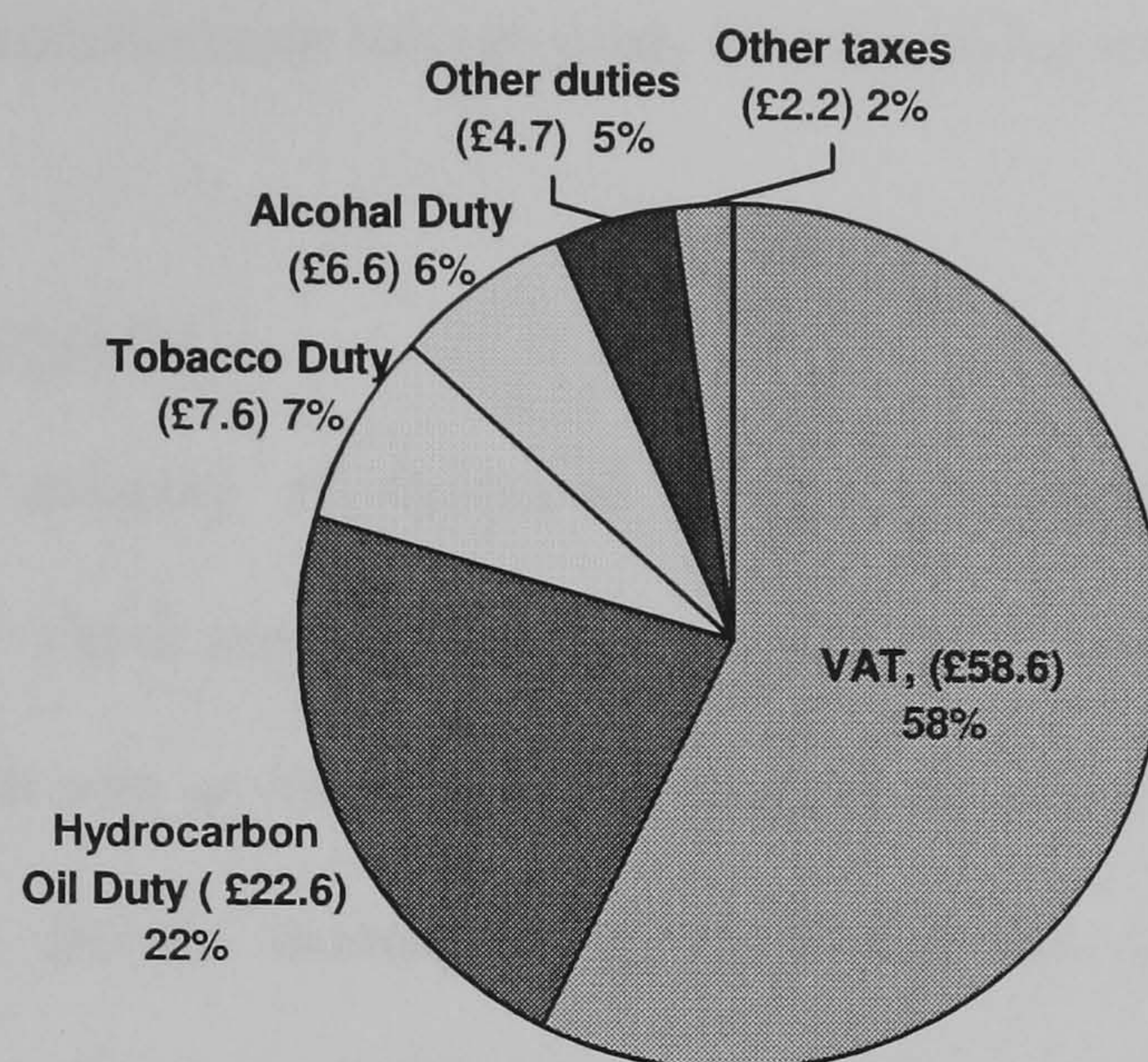
“HMCE exists to collect over a third of central Government revenue from indirect taxes and duties, to prevent smuggling and tax fraud, and to collect and analyse trade statistics” (HMCE, 2003a)

It takes pride in introducing itself as the organisation which contributes the major chunk of revenue to the central government:

“We raise nearly half of central Government revenue” (HMCE, 2002a).

The split of revenue collected is shown in the following fig 4.1:





Note: All figures are net. Total VAT collected was £101.2 bn. Repayments totalled £42.6 bn.

Fig 4.1: Total revenue collection by HMCE (Source: NAO, 2002: p 1)

However, the department performs more than mere tax collection function. Thus a more comprehensive classification of all the functions of the HMCE drawn from the official sources of HMCE (mainly HMCE, 2001a, b, 2002a, b and LSLO, 2000) is as following:

#### i. Revenue Collection

The first category is based upon the traditional role of revenue collection as already mentioned. However the emphasis upon *facilitation* and *friendliness* as opposed to pure *enforcement* is evident from inclusion of many enabling roles in this category. Those include helping people “to get their taxes right first time”. National Advice Centres and the official website are cited as the prime examples of this concern of the Department. Other functions manifesting the same



customer (tax payers) care concern are delivering its services electronically and helping international trade run smoothly by minimising red tape.

ii. *Law Enforcement*

The second category of functions pertains to *crime prevention* and *law enforcement*. These include fight against tax fraud and evasion evidenced by policies which aim at minimising the shadow economy and drugs trafficking, fight against money laundering, excise fraud and child pornography and providing protection to wildlife by fighting illegal trade in endangered species. The extent of enforcement work is reflected by the fact that the Solicitor's office of HMCE is the largest Crown Court prosecutor outside the Crown Prosecution Service (LSLO, 2000: 6).

iii. *Advisory Functions*

The third category of duties is *advisory* in nature. These duties include supply of statistical information about international trade that the Government and the European Union require for forming economic and taxation policies, and UK businesses for making their trading decisions. The Department also provides policy advice to ministers in connection with important decisions on taxation, revenue and other related policies. HMCE also remains engaged in promoting good practice in customs and tax matters around the world by having long-standing links with over 60 overseas taxation authorities, providing them advice and technical help.



In view of lack of proper understanding of the profile of the department and dearth of relevant published material, this chapter is devoted to defining a clearer profile of the department by linking the modern day HMCE with its historical origins.

## **4.2 Historical Background**

The revenue historians admit their inability to trace the exact origin of the Custom duties, describing them to be levied from “time immemorial” (Atton and Holland, 1967: p 1). However, a customs system is deep rooted in the ancient history of the United Kingdom, as a reference to "the ancient and rightful Customs" is found even in the *Magna Carta* (ibid: p 4). What all historians are unanimous upon is the fact that customs system is one of the most important historical legacies of the United Kingdom. Hoon (1968: p 1) observes that the English customs system inherited by the modern day HMCE served two purposes in the eighteenth century. First, as one of the most important cash generators, it brought vast sums into the Treasury. Second, it also enforced trade policy upon which protection and encouragement of industry and commerce depended. It can therefore be said that the pre-modern customs system, was an instrument for putting mercantile policy into effect at the British ports.

In the next sections the origins of the three mainstream taxes collected and enforced by the department have been briefly investigated

### **i. Customs System**

Custom duties are the earliest of the indirect taxes administered by HMCE. In early days the term '*customs*' applied to customary payments or dues of any kind; regal, Episcopal or ecclesiastical; until it became restricted to duties payable to the King upon export or import of certain articles of commerce (Carson, 1972, p 16). In those early times no uniform system existed for the collection of the customs revenue. The system was administered privately by the general practice of 'farming', which meant giving an enterprising merchant or courtier the right of collecting the 'duties' in return for a specified annual sum (ibid, 1972: p17), while in other cases the revenue was collected by officers appointed by the Crown or a local borough (Hoon, 1968: p 5 ).

The origin of a nation-wide customs system in England can be traced back to the Winchester Assize of 1203-4 when it was directed that the 'customary dues at the ports', should be accounted directly to the Exchequer, payable to King John rather than given to the local lords (Carson, 1972: p 16). Consequently, all sea-borne trade, both foreign and coastwise was properly recorded, with a sufficient description of the goods, the date of shipment and the name of the merchant concerned (Hoon, 1968: p 75). The next major development came in 1506 when a "book of rates" was established, which can be seen as the fore-runner of the present day Customs tariff (Carson, 1972: p 26).

By ordinance on 21 January 1643, the regulation of the collection of customs was entrusted to a parliamentary committee whose members were appointed commissioners and collectors of customs, forming a Board of Customs. This and succeeding committees appointed by Parliament until 1660, and thereafter by the



Crown, functioned until 1662, when those who had been serving as commissioners became themselves *lessees* of a new farm of customs. This continued until 1671, when negotiations for a new farm broke down, and a Board of Customs for England and Wales was created by Letter Patent (Hoon, 1968: p 6-7).

In 1809, a revenue force was established called the 'Preventative Waterguard', which brought the inland and offshore Customs officers together under the same wing. It was a collective term for the uniformed officers who searched ships and other transport as well as travellers' baggage (HMCE, 1983: p 28).

## **ii. Excise System**

The Excise Service originated in 1643 with the imposition of the first beer duty. Supposed to be only a temporary measure, called 'New Impost', to provide funds to continue the then civil war, it however soon became permanent (Carson, 1967 : p 40; HMCE, 1983: p 7). Charles II took the English Excise out of 'farm' and placed it under a Board of Commissioners of Excise in 1683 (HMCE, 1983: p 5). At first they covered a wide range of commodities, but when the duties were extended beyond the districts which parliament controlled to cover the whole country, they were confined to alcoholic liquor. Modelled after the Dutch Republic, the excise duty was settled by statute despite widespread protest in 1660. Excise duties spread to other commodities such as salt, paper, soap, candles and home produced spirits (NDAD, 2003).

### iii. VAT System

The political change that not only transformed the work of Customs and Excise officers but also their public perception was the introduction of VAT.

“On the first day of April 1973 all the lights at the front of the newly built Alexander House in Southend were doused. Then at a given signal switches were pulled and three gigantic letters blazed forth to lighten the surrounding darkness. The letters were VAT, and they proclaimed the introduction of a new tax. That tax was to change the image of HMCE (HMCE, 1983: p 65)

VAT is considered to be a European tax, not only because it originated there, but also due to the fact that it is one of the vehicles of harmonisation in the hands of economic policy managers with regards to the European Union. In France, a VAT had been introduced in April 1954 as part of the general tax reforms of 1954/55. Around the same time, the 1957 Treaty of Rome established the European Economic Community, thus materialising the idea of creating a single European market in the post-war Europe. Article 99 of the Treaty deals with taxation in particularly calling for harmonization of taxation in the interest of the common market, and Article 100 of the treaty authorizes the council of minister to issue directives for achieving harmonization (Ernst and Young, 1995: p 8).

In 1967, the council of minister adopted two directives which resulted in the implementation of VAT by all member states. The first directive provided that all member states replace existing cumulative sales tax system with a non-cumulative VAT system. The second directive introduced the basic concept (e.g., definition of taxable person, supply of goods and services etc). Further harmonization was however required to provide the European Union with its own financial means, as well as to eliminate fiscal frontiers in the future and



promote greater freedom of movement of people, goods, services and capital. That led to the Sixth Council Directive on VAT, effective as of May 1977, which provided for a uniform basis of taxation. The process of harmonization is helped by the work of the VAT committee of the EU established under article 29 of the sixth directive (ibid: p 9).

The French VAT of 1954 did not comply with the EEC Council's Directives because it applied to the transactions of manufacturers and wholesalers only and did not extend to the retail stage and services which were separately taxed. In January 1968 France, together with West Germany, introduced a full system of VAT complying with the Directives of the Council. A few months before this, in July 1967, Denmark, although not a member of the Common Market had introduced her own VAT. In January 1969, Sweden also introduced a VAT which was virtually at a single rate. Norway also followed suit in January 1970 by adopting a single rate structure VAT (Sandford et al., 1981).

### **VAT's Introduction in UK**

VAT replaced Purchase Tax and Selective Employment Tax (SET)<sup>37</sup> on 1 April 1973. Throughout its existence SET remained a controversial tax and the

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<sup>37</sup> Purchase Tax, a war-time levy (1940), applied to a wide range of consumer goods for the home market on wholesale stage, and was contributing some 9 % of central government revenue from taxation. One objection to the multi-rate structure of the tax was the arbitrariness of the classification on the basis of being 'luxurious' or not; another was that such arbitrary discrimination resulted in distortions. Being a wholesale tax, services remained outside its scope and so it could not provide uniformity across the board. SET, introduced in 1966, required every employer to pay the Ministry of Social Security a weekly sum for each employee in addition to the National Insurance contributions, the self-employed were excluded. Employers in manufacturing activities subsequently received a refund of payments, plus a premium. A second group of industries consisting mainly of agriculture, transport, mining, quarrying and fishing received a refund but no premium, while construction, distribution and service industries, received no refund; it was therefore on this latter group that the impact of the tax was primarily felt (Sandford et al., 1981: p 6).

Conservative Party was pledged to its repeal when it came to office in 1970. The first official body to examine the possibility of a VAT in the United Kingdom was the Richardson Committee. The Committee which reported before the introduction of SET, was asked to consider the replacement of either Purchase Tax or profits tax by VAT. Opposing both the changes, the Committee found VAT to be intrinsically much more cumbersome as a means of consumer taxation. However, Report of the National Economic Development Office (NEDO, 1969) and the Green Paper issued by the Conservative government in 1971, expressed its support for adopting VAT claiming that it would help improve the efficiency of resource use in the economy and do away with the shortcomings of Purchase Tax and SET. Although Conservative Ministers argued the case for VAT on its merits and held that they would have introduced it anyway, an essential background factor was Britain's impending membership of the EEC, which required the adoption of VAT as the Community's form of turnover taxation. Thus in 1972 the Conservative government passed legislation to bring VAT into effect from 1 April 1973 in place of Purchase Tax and SET (Sandford *et al*, 1981: p 7).

#### **iv. Other Taxes**

In addition to administering VAT, custom duties, and excise duties on alcohol, oil and cigarettes, HMCE is responsible for other numerous types of indirect taxes too (Annex 4.1 sets out details of those taxes, while Fig 4.1 provides a break-up of revenue for the major categories of taxes).



### **4.3 The Problem of Definitions**

HMCE is a large central government department employing 23000 workforce on average during last five years (See Annex 4.2 for various cadres' levels in the department). In order to understand the nature of HMCE as a public sector department it is necessary to first mark the distinction between the often interchangeably used terms like 'public sector', 'civil service' and 'executive agencies' which in turn would enable us correctly understand the place of HMCE within the central government hierarchy.

#### **a. Distinction Between *Public* and *Private* Sector**

By the term public we generally mean that part of the economy which is concerned with providing basic government services. However defining the phrase 'the public sector' is problematic as identified by Broadbent and Guthrie (1992) as well. The definition of "public sector" varies from one country to another and, indeed, varies over time within states. The broad definition of the public sector given by Massey (2002) is:

“anything in which the state has an interest and public money follows, but this would include many voluntary (not-for-profit) and private sector organisations which receive public money and deliver services on behalf of central and local government”.

The more restrictive meaning of the term 'public sector' can however be found by making reference to the governmental level accounting practices. For instance, Black *et al* (2002: p 40) outline the official distinction between public and private sector for government's balance sheet purposes as:



Public sector

This comprises general government, public non-financial corporations and the Bank of England.

Private sector

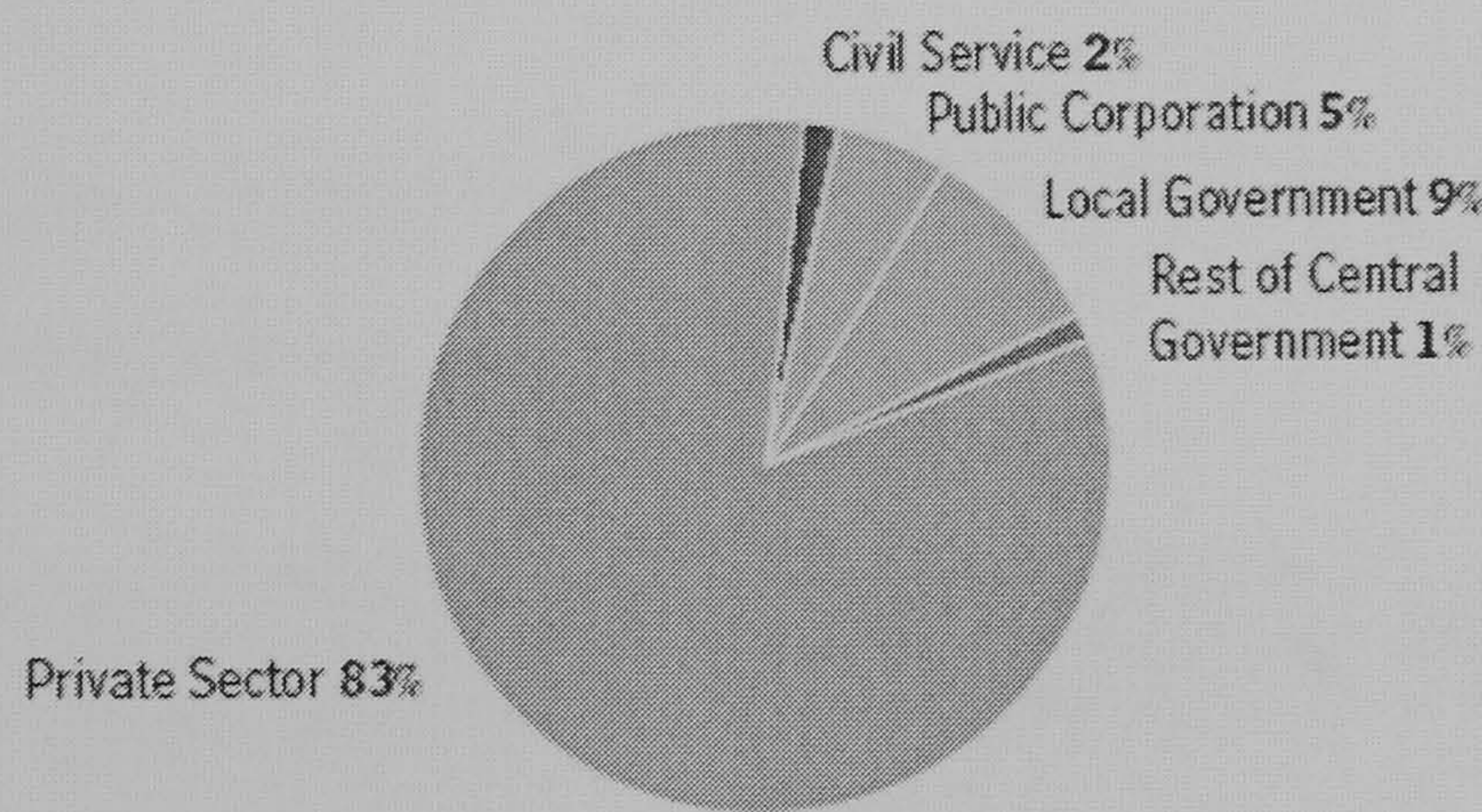
This comprises private non-financial corporations, financial corporations other than the Bank of England (and Giro bank when it was publicly owned), households and the NPISH (non-profit institutions serving households) sector.

- The definitions of the sectors comprising the public sector as mentioned in the above definition have also been elaborated in the publication. For sake of clarity, relevant sections have been reproduced in Annex 4.3

As per official statistics, the public sector in the U.K accounts for approximately 17% of the total employment on head count basis. Civil service which is a part of the public sector accounts for 2% of total UK employment, and 10% of the public sector.

**EMPLOYMENT IN THE PUBLIC AND PRIVATE SECTOR,  
UK JUNE 2000**

Employee jobs – headcount basis



SOURCE: MANDATE, DEPARTMENTAL RETURNS AND ECONOMIC TRENDS

Fig 4.2: Public Sector as % age of total UK workforce (source: Cabinet Office, 2002a: p 4)



### **b. Distinction Between Civil Service and Executive Agencies**

Historically the *Civil Service* has grown out of the administrative staffs of royal households from Anglo-Saxon times onwards, however the organisation that is recognised as the modern civil service took shape between 1850s-1920s (Pyper, 1995: p 5-6). The *Civil Service* in 1980s had grown into a unitary organisation which was characterized by its adherence to certain key percepts like permanency, neutrality and ministerial responsibility (ibid: p 12).<sup>38</sup>

The ‘executive agencies’ were introduced by the Thatcher government as a result of recommendations made by a report titled “*Improving Management in Government: The Next Steps*” (Ibbs Report, 1988).<sup>39</sup> The report recommended that decentralized agencies should deliver executive functions of government “within a policy and resources framework set by a department”. The report also recommended that under new arrangements the Departments should maintain their traditional policy support role offered to ministers but would have to develop new roles establishing and managing a policy and resources framework with agencies.

The New Labour government did not dispense with the plan as is evident from the foreword to the Next Steps report, 1997.

“I have watched with interest the development of the Next Steps Project since its launch ten years ago. The Project represented an attempt to reorganise the way in which the Civil Service does business around sound principles of delegated management, and the Labour

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<sup>38</sup> The Civil Service comprises all government departments and executive agencies in Great Britain and includes the Diplomatic Service (Cabinet Office, 2001a: p 2).

<sup>39</sup> The report produced by a committee comprising Kate Jenkins, Karen Caines, Andrew Jackson, on behalf of Efficiency Unit of the Prime Minister’s Office had concluded that the existing civil service, due to its unitary and centralized structure, was geared towards prioritizing its policy responsibilities towards ministers at the cost of service delivery to the intended users. The report thus had proposed a split between policy formulation and service delivery.

Party was therefore happy to support it in Opposition as well as now in Government” (Next Steps Report, 1997).

Therefore it can be seen that executive agencies are part of the *Civil Service*. But they have delegated authority to employ their own staff and organise service provision in ways best suited to meet customer needs. They have to work under the terms of individual framework documents and subject to overall budgets agreed with their parent department and/or the Treasury. Agencies are headed by chief executives who are personally responsible for day-to-day operations. They are normally directly accountable to the responsible minister, who in turn is accountable to Parliament. Almost 76 per cent of civil servants now work in Next Steps agencies (Cabinet Office, 2001a: p 4).

As on 1 April 2001 there were 93 executive agencies in the Home Civil Service, while four departments operate on Next Steps lines. HMCE is one of them, while the remaining three are Crown Prosecution Service, Inland Revenue and Serious Fraud Office (ibid).

The difference and similarities between a department and executive agencies have been made clear in this section. The understanding helps in stating now that HMCE is a Department of State which works on agency lines. The department started to work on Next Steps lines on 1 April 1991.

### **c. Relationship with HM Treasury**

HM Treasury is responsible for formulating and putting into effect the UK Government's financial and economy policy. The Treasury has a strategic oversight of banking, insurance and financial services and is responsible for the Government Accountancy Service which brings professional accountants in



government together. The Treasury is also the lead department on government statistics, which are independently produced by National Statistics. In addition to these functions, the Treasury is also entrusted with promoting a fair and efficient tax and benefit system. Direct taxes are collected by the Inland Revenue, while the indirect taxes, as already mentioned, fall within the responsibilities of HMCE (HM Treasury, 2003a).

The Treasury is headed by the Chancellor of the Exchequer who has overall responsibility for the work of the Treasury. He is assisted in his managerial work by Chief Secretary to the Treasury, Paymaster General, Financial Secretary and Economic Secretary. The *Paymaster General* looks after strategic oversight of taxation as a whole, including overall responsibility for the Finance Bill, closer working between Inland Revenue and HMCE (including with other departments), and European and international tax issues. He is also the Departmental Minister for Inland Revenue and the Valuation Office.

The *Economic Secretary* is the Departmental Minister for HMCE. The Treasury in its annual report sets out the performance of seven Departments which report to the Chancellor or his ministerial colleagues. However HMCE and the Inland Revenue, being larger departments produce separate reports (ibid).

#### **4.4. Organisational Structure**

##### **i. Medieval Days**

In 1275 Edward I imposed what was referred at the time ‘new custom’. The ‘farm’ for these levies was allocated to the merchants of Lucca (Carson, 1972: p 17). The ‘farmers’ would appoint their own officials in the port who were known

as 'collectors'. The three principal Crown officers in the medieval days were the *customer*, *controller*, and *searcher*, who were originally appointed by the King or by the Chancellor, Treasurer, King's Chamberlain, Barons of the Exchequer, and others, and their term of office was during pleasure only (Hoon, 1968: p 5). The king's officials acted as a check upon the account of goods.<sup>40</sup> 'Customers' were set up in 1297 who were required to receive monies transmitted to them by the collectors and to make payments as directed by the Exchequer. The office of 'searcher' was established two year afterwards with duties of assisting bailiffs in arresting persons, examination of export goods and preparation of accounts (ibid: p 18).

Hoon (1968) highlights the administrative muddle in which the customs system had descended before the start of 18th century. With the end of the practice of farming in 1671, the 'collector', originally the servant of the 'farmer', became a Crown officer. The office of collector was thus gradually introduced and extended over the whole department, and to the collector was also given complete responsibility for the collection of duties in a port and for the return of money and accounts into the customs office. With the controller, he had the general superintendence of the port as well. The customer, who then no longer had charge of the collection of duties, remained, it appears, mainly for the purpose of returning into the Exchequer the accounts required of him and of directing the coast business in which the farmers had no concern. The controller continued to act as a check on the collector. The activities of the searcher became confined entirely to the export business (Hoon, 1968: p 7)

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<sup>40</sup> The account used as a check on the collector's account was made on a counter roll, thus the officials began to be called 'comptrollers' or 'controllers' (Carson, 1972: p 17).



## ii. Modern Day HMCE

In the official publications HMCE is presented as a single department administering indirect taxes. The senior management structure as outlined in such publications also fails to underscore the heterogeneity and complexity in the work of the department. From the review of historical background of the department it must be clear that the existing department is made up of three different work regimes which were distinct departments in the past. A memorandum submitted to the Select Committee on Treasury also refers to this concealed reality:

“The first thing that the Committee must recognise is that there are three Customs & Excise Departments administering three different taxes (hereafter referred to as Customs, Excise and VAT). There are vast differences between the administration, collection, enforcement procedures, compliance and legal statutes affecting each Department. This makes it very difficult for the Departments of HM Customs & Excise to work under one umbrella and closer co-operation and a more integrated approach to trade and the public are issues that are constantly under examination” (TSC, 2000a)

A senior level manager also points to this fragmented profile of the department.

“we are a strange outfit, as much Customs and Excise is strange as it doesn’t have a single HQs like many organisations do; there are offices like the one in London where the Board sits, the VAT operations in Liverpool, and in Manchester which is our Excise operations hub, and Southend which is where International trade and Customs have their hub” (SO1)

“the approach is mirrored, if you like, in all functions, so there is an Excise performance team in Manchester; of VAT in Liverpool and also of Customs and International trade, a similar one” (ibid)

It is therefore helpful to remember that the department essentially comprises three distinct work patterns, i.e. customs, excise and VAT even in its regular revenue collection role. On the law enforcement side two major categories can be identified. First, *crime prevention* related activities like anti-drugs, anti-money

laundering etc and second, anti- evasion of legitimate revenue related activities e.g. preventing *Missing Traders Fraud* or smuggling of dutiable items.

HMCE was reorganised in 2001 along functional lines. But before the existing structure is explained, first the structure before those reforms is discussed.

**a. Before Re-organisation of 2001**

Operational work for the purpose of local control and collection of Customs and Excise was carried out by several geographical regions, known as *Collections* (Executive Units). In 1970 there were 30 such regions but these were gradually reduced, and in 1995 a major reorganisation of HMCE resulted in the number of regions reduced to 14 geographical regions in the United Kingdom.<sup>41</sup> A Collection was divided into a number of districts, depending on the concentration of customs and excise work. Four Headquarter sites dealt with policy and some centralised operations. Each Collection was under the control of a Collector who was the Board's personal representative in that Collection.<sup>42</sup> The Waterguard, administered separately before 1971, enforcing revenue control on the flow of ships and aircraft, and their passengers and crews, in and out of the UK, was also amalgamated with the Collections (NDAD, 2003; Simpson and French, 1998).

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<sup>41</sup> The Collections consisted of Northern Ireland, Scotland, Northern England, North West England, Eastern England, Wales, the West & the Borders, Central England, Anglia, Thames Valley, London Airports, London Central, South London & Thames, Southern England and South East England.

<sup>42</sup> The Collector was supported by a team consisting of a Deputy Collector and Assistant Collectors, each of whom headed an operational division dealing with a specific geographical and /or functional area.



### **b. Structure in 2003**

On 17 January 2001 the new Chairman of the department, Richard Broadbent, announced significant changes in the organisation and senior management of HMCE, to be fully implemented from 1 April 2001. The intended purpose of those changes was to reflect the changes in the approach to management, HR and resource allocation. It was claimed that the reforms intended to create greater clarity and focus around how the department performs its core activities, simpler and more empowered management structures and a clearer relationship between its support activities and the front line (HMCE, 2001a).

The department was reorganised into two main operational arms, *Business Services and Taxes* and *Law Enforcement*, which are served by Support functions- *Finance, Legal, Logistics and Human Resources (HR)*. The two main operational arms have separate regional management arrangements, detailed below.

#### **i. Business Services and Taxes (BST)**

*Business Services and Taxes* manage dealings with legitimate businesses, being responsible for the administration, collection and policy of all business taxes, international movements and trade services. It has approximately 13,000 staff. Most services though continued to be delivered regionally, but some (such as services to large traders) were, for the first time, managed centrally.

BST is further made up of four units

*Policy Group* consists of two Directorates - *Customs and Tax Practice* and *Policy Development*. The Group is managed as a single entity. Both the *Joint VAT Consultative Committee* and *Joint Customs Consultative Committee* fall within this Group.

*Tax and Customs Practice* maintains policy by framing rules; designing technical legislation and defending it against avoidance and litigation; providing clear and timely guidance to operational staff; and developing professionalism through technical training and standards. It contains most of the former VAT Policy Divisions and new Divisions made up from the former Excise Policy Group and from Trade Policy.

The *Tax and Customs Practice* management team looks after International Trade, VAT Commercial, VAT Supply, Professional Standards Service Standards, Environmental Taxes Regime, Alcohol, Tobacco & Gambling Regimes, Compliance Framework

*Policy Development* is responsible for the development of policy for Business services and taxes. It works closely with Ministers, Government Departments, and others, including the business community, and in the international arena, including the EU. It consists of a new *Tax Strategy Division*, *International Division*, two new *Policy Divisions* created from the former Excise Policy Group, and VAT Social.

The new *Customs and International Trade Division* brought into Policy Group some work from the former Enforcement Directorate on restricted goods, and from Delivery on customs procedures. And some cross-cutting tax work (for



example, on penalty regimes) got concentrated in the new *Compliance Framework Division* in Liverpool, which spans excise, VAT and customs, and supports the two operational Directorates in BS&T: *Large Business Group* and *Regional Business Services*.

*Large Business Group* is managed from the centre, and is responsible for the collection and control of UK taxes and duties from the largest businesses in the UK. It is also responsible for Closer Working with the Inland Revenue. The Group consists of five large business regions, computer audit, and a Large Business National Office.

*Regional Business Services* is responsible for all aspects of those business services which are delivered regionally (i.e. those other than for large businesses), including operational policy, resourcing, guidance and delivery. RBS includes all VAT and excise assurance staff (except those in Large Business Units); VAT sift teams, including risk managers; cash and shadow economy teams; entry processing units; operational policy; guidance; risk analysis; credibility and resourcing formerly in Delivery Directorate; credibility formerly in Logistics; contact centres; business education and liaison.

There is also a *Business Design* directorate, which is responsible for systems, controls and managing major changes in business structure and organisation. Business Design consists of three teams, responsible respectively for large business change projects (e.g. Debt Management and Registration / Deregistration); working with the rest of BS&T and with Logistics Directorate to develop the strategy for the implementation of the new systems for an e-business

environment; and supporting the management team to ensure a smooth transition from the current systems to the new environment.

## ii. Law Enforcement

The other operational arm of the department, *Law Enforcement* contains all investigation, intelligence and detection activities (both national and regional), along with their supporting business operations and policy functions. Its focus is on fraud or other breaches, where any business activity that exists is incidental to the main (unlawful) purpose of the activity. It has approximately 8,000 staff.

*Law Enforcement* consists of five units:

*Investigation*, comprising all investigation resources, both national and regional, including investigation staff previously in Collections (such as LFUs) and Task Completion Units. *Intelligence*, comprising all intelligence resources that were formerly in Collections and in Central Intelligence.<sup>43</sup> *Detection*, consists of anti-smuggling staff, Excise Verification Officers, red point staff, freight examination staff and Road Fuel Testing Units. The *Regional Detection* management team consists of heads of regional offices. *Policy*, which identifies law enforcement priorities for strategic analysis and research, and develops strategies for the delivery of anti-fraud outcomes and targets, working closely with the key external policy agencies.

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<sup>43</sup> The *Intelligence* management team, consists of Head of Regional Intelligence, Head of Operations & International Intelligence, Head of Intelligence South, Head of Intelligence North, and Head of Intelligence Central



*Business Design*, which is responsible for systems, controls, the definition of business requirements from support and management of business change processes. It consists of a single unit, based in London.

### iii. Support Functions

The two operational arms of the department are served by four central support functions:

*Logistics* comprise all technology staff, both national and regional; e-business, corporate services; information management; banking; projects; estates and purchasing. *Finance & Strategy* comprises finance and planning; accounting; analysis; communications; internal audit; internal investigations; governance and structure; business design; and a new command covering cross-cutting legal and parliamentary issues. *Human Resources (HR)* covers personnel management; pay and industrial relations; training and development; personnel advice and services. It also took over management of the former HQ personnel management units and training & development units.

The composition of, and management arrangements for *legal* services (The Solicitor's Office) remained unchanged (see Annex 4.4 for a diagram of organisational structure).

[Sources : HMCE intranet, Minutes of JVCC, 2001, HMCE, 2001,a,b,c]

## **4.5 The Board and Senior Management**

### **i. Evolution of the Board of HMCE**

From very early times and more particularly from the reign of Henry VI, the customs establishment had been under the governance of the Lord High Treasurer but during the seventeenth and eighteenth centuries, at such times as the Treasury was put into commission and after 1714, when the Treasury was permanently in commission, the Lords of the Treasury took over the control of the organisation. The Treasury formed a connecting link between the Customs Board and Parliament, the Council, and other departments of state. By the patent which created the Board of Customs, the Commissioners were directed to follow the directives given by the Lords of the Treasury or the Chancellor of the Exchequer when the Treasury was not in commission (Hoon, 1968: p 46-50)

The Board of Customs Commissioners which was instituted by patent in 1671 consisted of six Commissioners though the number was increased to seven two years later and varied between five and nine during the first hundred years of the history of the commission. An important development of the eighteenth century was the gradual, almost imperceptible, evolution of the Board of Commissioners as the fountain of all authority within the department (ibid: p 56-60)

The number of Commissioners who attended the Treasury varied. The chairmanship of the Board was determined in 1705 by the Commissioners agreeing to act in rotation, an arrangement that apparently was continued until 1788 when two warrant chairmen were appointed to preside at all meetings of the Board, to be relieved only Mondays in the winter and Saturdays and Mondays in



the summer by other Board members in rotation. This would appear to have been the first step towards the establishment of the permanent chairman of modern times (ibid: p 73)

Cooperation between the Customs and Excise Boards was a necessity. There were several foreign commodities, notably tea, coffee and brandy which were subject to excise duties as well as customs duties, and the officers of both departments were employed in their collection. It was upon the cooperation between the practical officers of both services that the relationship of the Excise and Customs Boards depended. However despite the best efforts of the Commissioners of both departments wrangling between the two departments over seizure powers continued without end. The Custom Board's direction to one collector "to enjoyn & recommend it to all the officers of your Port to behave decently and to live in unity and harmony with the Officers of Excise" betrays well the situation which then prevailed (ibid: p 86-88)

In 1833 a Royal Commission on Excise was appointed by Letters Patent to inquire into the establishment of the Board of Excise, and into the management of a collection of excise revenue in all branches throughout the UK. Its twentieth and final report was issued in July 1836. In 1849, the Board of Excise combined with the Board of Stamps and Taxes to become the Board of Inland Revenue (NDAD, 2003).

In 1908, the management of duties of excise and of the relevant powers and duties of the Commissioners of Inland Revenue were transferred to the Commissioners of Customs. The Commissioners of Customs were thenceforth called The Commissioners of Customs and Excise. The Customs and Excise

Services were amalgamated as an order in Council from 1 April 1909, and were administered by the Board of Customs and Excise and became known as Her Majesty's Customs and Excise (NDAD, 2003)

The Chairman of the Board of Commissioners is the head of the Department. The 1979 Customs and Excise Management Act (CEMA, 1979) consolidated the collection and management of revenue of customs and excise. The Act neither mentions nor specifies any statutory functions to the Board. The day to day management of the Department is the statutory responsibility of the Commissioners along with other statutory functions.

The Chairman, Director General (*Law Enforcement*), Director Intelligence (*Law Enforcement*), Director General (*Business Services & Taxes*), Director (*LBG*), Director (*RBS*), Director (*Logistics & Finance*), Director (*Information & e-Services*) and The Solicitor as the executive Directors, and five non-executive Directors together comprise the Board. Assisted by three sub-committees<sup>44</sup>, the Board meets once a quarter to review the strategic issues facing the Department and to provide advice and guidance.

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<sup>44</sup> In a simplified structure put in place in April 2000, these sub-committees replaced a large number of formal and ad hoc committees.



<div>Chairman</div>		
Executive Directors		
Law Enforcement	Support Functions	Business Services & Taxes
1. <i>Director General</i>	3. <i>The Solicitor</i>	6. <i>Director General</i>
2. <i>Director Intelligence</i>	4. <i>Director (Logistics &amp; Finance)</i>	7. <i>Director LBG</i>
	5. <i>Director (Information &amp; e-Services)</i>	8. <i>Director RBS</i>
5 Non-executive Directors		

Fig 4.3: Composition of the existing Board of HMCE (HMCE, 2002d: p 12)

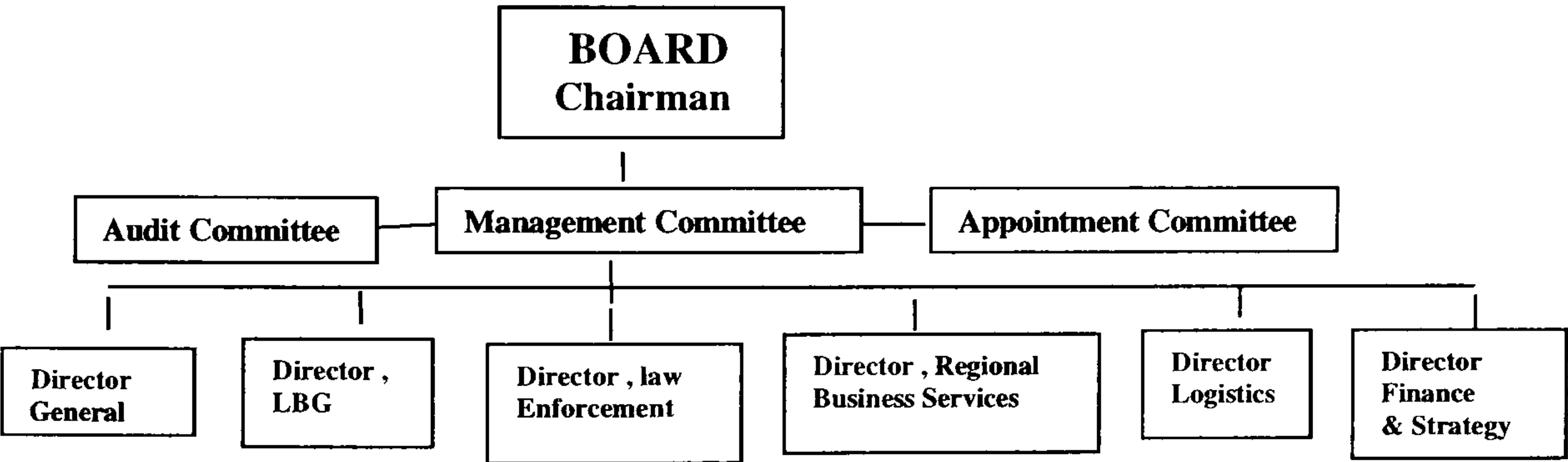


Fig 4.4: Board level existing committee structure of HMCE (NAO, 2002c: p R9)

The Chairman of the Board of Customs and Excise corresponds in rank to that of Permanent Secretary, and the Deputy Chairman to that of Deputy Secretary. The Commissioners, whose rank corresponds to Under Secretaries, and form the Board of Customs and Excise, have a corporate responsibility, but are each responsible for an assigned segment of work. They are all directly responsible to the Chancellor of the Exchequer (NDAD, 2003).

As a part of restructuring all regional Committees were abolished and instead a single Regional Management Committee comprising the heads of the 13 regions

plus the Chief Investigation Officer of National Investigation was set up which is responsible to the Management Committee. The stated objectives of the Regional Management Committee are to improve communication and co-ordination between the centre and regional management and to act as a single channel for initiatives from the centre to the regions. The Solicitor is responsible and answerable to the Chairman and to the Board. He is not a member of the Management Committee, but attends its meetings when legal questions or issues which concern his Office arise. The reorganisation included setting up a single national unit responsible for all the indirect tax and customs affairs of the UK's largest businesses numbering around 1,000 and accounting for over half the total revenue collected by the Department. The regional formations were to deal with businesses other than those included in the large businesses unit (TSC, 2002a).

#### **4.6 Conclusion**

The analysis of historical origins of the indirect taxes and the organisations which administered them establishes that complexity of functions is a historical legacy of HMCE. Moreover, the law enforcement origins of HMCE explain the present day ethos of the organisation as the organisation is generally perceived as a law enforcement organisation. In the NPM inspired literature, 'customer-focus' is the focal notion where customer is the recipient of services. But, interestingly, in the case of HMCE, 'customer' used to be a tax official in the medieval days. The 'customer-focus' in its modern sense is not a well developed policy concern in HMCE. How this ethos was desired to be changed by NPM inspired accounting changes is the central theme of next chapters.



## Chapter 5

### **Accountability for Performance in a tax administration**

#### **Introduction**

In this chapter a general framework of classifying accountabilities and PMSs of tax authorities is drawn. This is done with the help of referring to performance measures used by various tax authorities for reporting their organisational performance. The PMS of HMCE before 1997 is then analysed and its positioning on the proposed continuum is identified. This positioning is important as the accounting changes discussed in the subsequent chapters aim at moving the PMS from one type to another.

#### **5.1 Performance Measurement in a Tax Administration**

It was noted in Chapter 2 that ‘performance’ is a notion which can be interpreted differently by different stakeholders of an organisation (Otley, 1999). So before performance is measured it is important to ascertain how it is conceptualised by the management of the organisation. If performance measures are viewed as the ‘*constructs*’ of the notion of performance, these can be used to answer how performance is visualised by the management. It is therefore important to gain some understanding of different ways in which performance can be conceptualised in the case of tax authorities before the specific case of HMCE is analysed. For that purpose three examples of how performance is officially reported by different tax authorities in the world are briefly reviewed here. The

review is then used in proposing a categorisation of PMS used by tax authorities. But before a categorisation is proposed it is important to define a few key ideas and terms related to the analysis.

The 3Es (economy, efficiency; and effectiveness) model is the most talked about framework of public sector management. The model is based upon a simple *input, process* (or *activity*) and *output* model of organisations (Boland and Fowler, 2000; Pollitt and Bouckaert, 2000; Flynn, 1997; Rouse, 1999; Carter et al., 1995). Input resources are identified by Boland and Fowler (2000: p 419) as physical, human (staff and clients/cases) and financial where financial inputs are argued to be the most important as acquisition of other resource types usually depends upon the funds available. The authors argue that measures commonly used in public sector organisations are based on derivatives of this ‘economy’ or input oriented perspective, which are usually expressed in terms of cost, budget and staffing totals. It is also argued that any change in these performance measures (e.g. cost per case, cost per service type, numbers and categories of staff involved) simply reflects the ‘economy’ with which the organisation is using its resources but provides little information about the operational processes within the organisation, apart from some crude benchmarking. Outputs of organisations can also be easily measured in quantifiable terms and the authors give examples such as ‘patients treated’, ‘crimes solved’, ‘students gaining various qualifications at different grades’, ‘children placed in foster care’. The ratio of input to output is defined by the authors as a measure of organisational efficiency where an increase in the number of outputs, for a given input, simply demonstrates how efficiently an organisation is converting its inputs into outputs.



Pollitt and Bouckaert (2000: p 12) define ‘process’ as the activities which take place inside the organisation in order to generate outputs.

Boland and Fowler (2000: p 420) contend that public sector organisations are created to meet some perceived societal need. ‘Outcome’<sup>45</sup> is defined by the authors as the impact that outputs have in meeting the perceived societal need, while ‘effectiveness’ is defined as the extent to which outputs meet such needs and requirements<sup>46</sup>. Pollitt and Bouckaert (2000: p 12) state that outputs interact with the environment to produce ‘outcomes’ and distinguish between ‘intermediate outcomes’ and ‘final outcomes’. The former are termed ‘results’ while the latter are termed ‘impact’. The authors present the 3Es model as input/output model reproduced as Fig 5.1

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<sup>45</sup> The authors identify three main reasons for making measurement of ‘outcome’ difficult. First, ‘outcome’ is generally thought of in qualitative terms. Second, the process is also frequently complicated by the length of time it takes for such impacts to be identified. Finally, the impact of outcomes arising from the actions of other agencies, working in related policy areas, adds further complexity, e.g. welfare services and health.

<sup>46</sup> The authors argue that it is much more difficult to assess effectiveness, let alone measure it and that it is debatable whether simply increasing the number of, and measurement of, outputs, will automatically result in the meeting of such needs?

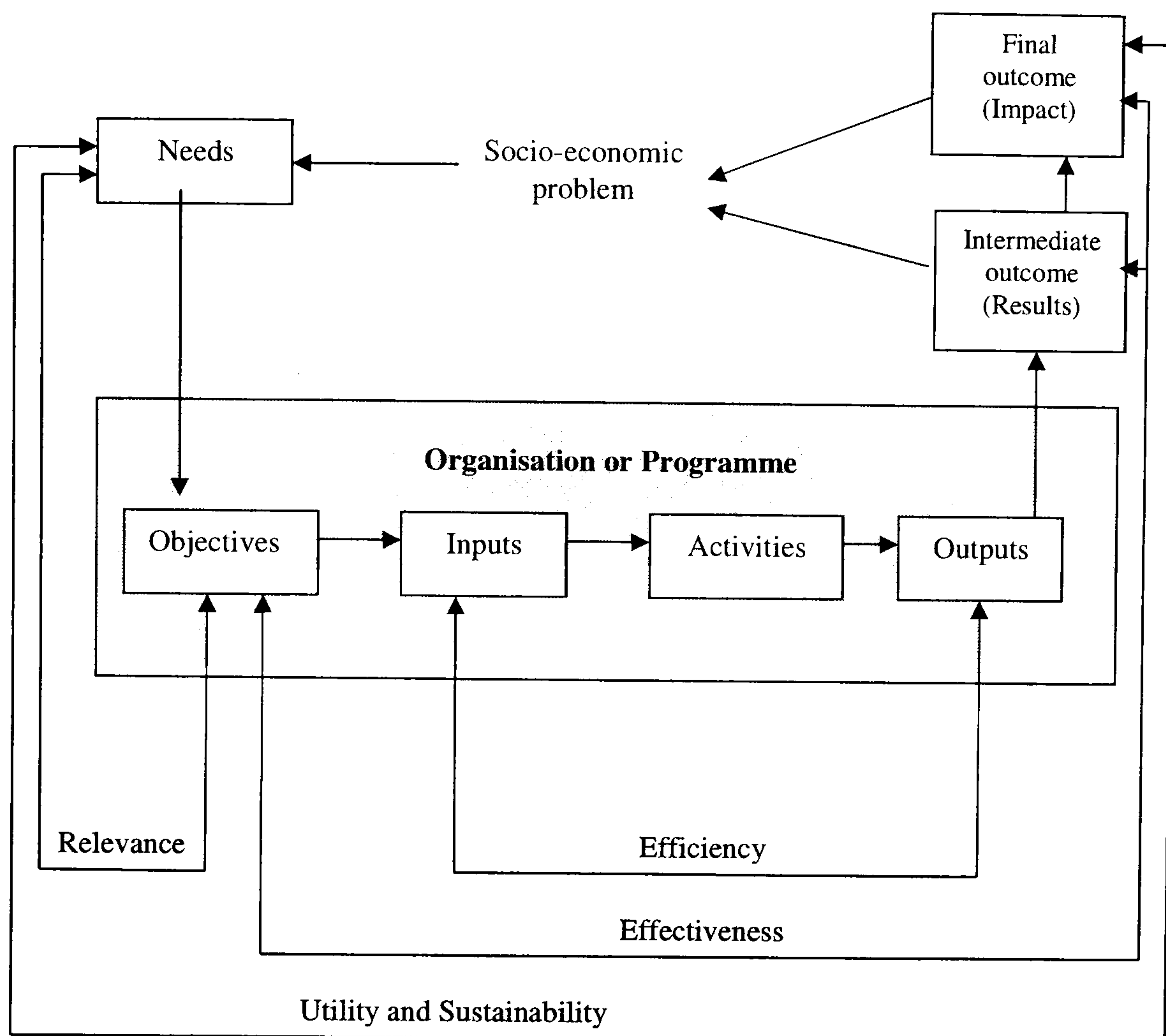


Fig 5.1: Input/Output Model (Pollitt and Bouckaert, 2000: p 12)

The key terms like inputs, outputs, process, outcomes and effectiveness with regards to public sector organisations have been defined. Now a generic classification of PMS of tax authorities is proposed with the help of a brief review. The review begins with the performance reporting of the organisation where this PhD researcher has worked i.e. the *Central Board of Revenue* (CBR), the tax administration of Pakistan.<sup>47</sup> The organisational performance in CBR is reported solely in terms of meeting revenue collection targets and cases of anti-

<sup>47</sup> The PhD author has himself seen and experienced the importance of this traditional form of performance reporting. In fact many chairpersons of the tax department of Pakistan lost their jobs prematurely because the revenue figures were not met.



evasion<sup>48</sup>. The nature of performance reporting can be judged from the following lines appearing in one quarterly report

“CBR has achieved the revenue target of the first nine months of the fiscal year 2002-03. The July-March net collection stands at Rs. 310.3 billion against the target of Rs. 310.1 billion. The task of achieving the revenue target for the first three quarters of current financial year has been accomplished in a forthright and straightforward manner” (CBR, 2004: p 4).

The media coverage given by the department on its performance is also in terms of revenue collection. For instance “*Rs 62.4 billion taxes collected in two months*” is the headline of a report published in the widely read national daily *The Dawn* and the financial daily *The Business Recorder*, on 1-9-2004. Similar reports keep on appearing in the national press on monthly basis.

This type of PMS can be termed as the ‘traditional’ form as ‘performance’ is reported with the help of revenue collection figures, which are the direct and immediate outputs of the activities of a tax administration. This can be compared to sales and profit figures which have been traditionally used by the private businesses to measure and report their performance.

In Chapter 2, performance was defined by Brumbach (1988) in terms of *results* and *behaviour*. Good results can be achieved with either good or bad behaviour. If good results are caused by good behaviour ‘performance’ is termed a *positive success*, while performance is termed a *negative success* when the same results are achieved with a negative behaviour. Tax authorities also learn that good revenue collection figures can be achieved with either good or bad behaviour. While negative success may be good in the short term, it can lead to lack of trust and good relations between the tax collectors and tax payers which is detrimental

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<sup>48</sup> The department publishes quarterly and annual reports of performance, which can also be accessed at its official website [www.cbr.gov.pk](http://www.cbr.gov.pk)

for revenue collection figures in the long run. Arguably, when a tax administration considers ‘positive success’ more important than mere good revenue figures, it adds performance measures/PIs in the formal performance reporting system relating to behavioural aspects. However, the traditional output measure of ‘revenue collection’ remains the most important measure of organisational performance. Examples of these additional measures are Citizen Charter standards<sup>49</sup> like *Number of calls returned within 3 working hours*, *Number of full replies within 10 working days*, *Number of appointments kept within 10 minutes of the agreed time*. HMCE’s performance reporting before 1998 is a good example of this form of performance reporting which will be discussed more in the next section.

The case of *Swedish Tax Authority* leads us to identify another form of PMS in tax administration (OECD, 2001: p 6). As the tax authorities are exposed to greater strategic management approach, they start thinking in terms of strategic goals of the organisations. They also define the ‘outcomes’ which a tax organisation aims to achieve. In terms of 3E model, there is greater recognition of, and emphasis upon the third ‘E’ i.e. *effectiveness*. The important change is that revenue collection figures are not reported as the measure of performance. Instead PIs which reflect performance with regards to ‘outcomes’ are used for performance reporting. It is possible that revenue collection or its derivatives may remain one of the outcomes. But what is important is that performance becomes a multi-dimensional notion where revenue collection is one of the dimensions of performance. For a long time, the performance of the tax administration was reported in the form of an *Annual Report* which remained

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<sup>49</sup> For a complete list of Charter Standards of HMCE see Annex 5.1



focused on a few performance indicators. In 1994, upon the government's directive, the National Tax Board redefined its performance. The Board termed the new PMS as *Performance Measurement Model* (PMM) which was built around the *input-activity-output-outcome* sequence discussed earlier in this section. Three basic performance criteria were defined in the new PMS: *productivity, quality and effectiveness*. The first outcome of *total productivity* is defined as output over input. Output is defined as a weighed total of tax returns, field audits and corrections due to desk audits, while inputs are defined as cost and work hours. The second outcome of *quality* has two definitions; quality according to legal and professional standards and quality according to taxpayer perceptions. The former is assessed by frequency of certain errors, timeliness, standard of quality assurance systems etc, while the latter is measured using taxpayer surveys. The third outcome of *Effectiveness* has been defined as the tax administration's *impact on the tax gap*. The tax gap<sup>50</sup> was then divided into *collection losses* (taxes billed but not collected) and *assessment error* (theoretical tax minus the total tax bill).

The three examples of different types of PMS in tax authorities show that performance reporting in the context of tax authorities can be seen as ranging from pure traditional form (i.e. revenue collection) to multidimensional outcomes reflecting some semblance of Results and Determinants of Fitzgerald et al.

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<sup>50</sup> The Tax Gap is the difference between the amount of tax that is due on a given volume of economic activity if taxpayers comply with both the letter and the spirit of the law and the amount of tax we actually collect from that economic activity both routinely through the operation of the normal tax collection processes and subsequently through various kinds of recovery activities – pursuing inquiries, chasing up unpaid tax etc (HMRC, 2005).

(1991) or Balanced Scorecard (BSC) of Kaplan and Norton (1992).<sup>51</sup> It is important to remember that terms like ‘results’, ‘outcomes’, ‘effectiveness’ and ‘quality’ do not have standardised meanings and one tax administration can use these terms entirely differently from the way another tax administration defines them. However, informed by the examples of different types of PMS included in this section, a generic classification of PMS can be proposed in the form of the following figure.

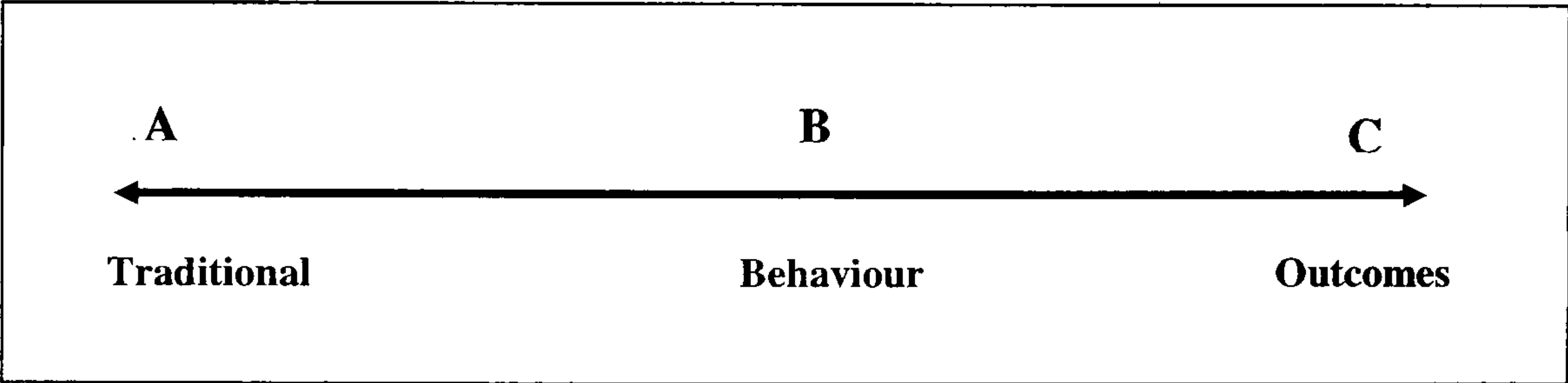


Fig 5.2: A classification of PMSs of tax organisations

At one extreme (point A) are the tax authorities that measure only revenue collection figures (and cases of anti-evasion) for reporting organisational performance. Such a PMS can be termed as ‘Traditional’ because revenue collection has remained the traditional definition of organisational performance. In terms of accountability relationships, it can be argued that such organisations consider the resources provider (i.e. government) as the only dominant stakeholder. Since no data is made available to the taxpayers which can help them assess the organisational performance from their perspective, their ability to exercise accountability powers are seriously curtailed. Of course, the taxpayers can use other channels of influence, e.g. print and electronic media, and pressure groups. But the fact remains that PMS itself does not act as a tool of

<sup>51</sup> This theme will be further picked up in later chapters.



accountability for the taxpayers in such a type of tax administration. In this form, the tax authorities view performance as a one-dimensional notion. If tax collection figures are up, and/or revenue targets met, then performance is viewed as good. Not only issues of quality (e.g. taxpayers' satisfaction) are not included in the PMS but even 'productivity' is not measured and reported. The case of tax administration of Pakistan (i.e. CBR) cited earlier is an example of this category.

At the other extreme of the categorisation (i.e. point C) labelled 'outcomes' are the PMSs which, arguably, reflect the influence of NPM. In such organisations the performance measures/PIs are based on clearly defined 'outcomes'. Their key distinction from the 'traditional' PMS is that the 'outcomes' targets and PIs not only relate to the concerns of tax collectors but they also accommodate the concerns of taxpayers as well. The PMS comprises measures/PIs related to revenue collection or its derivatives (reflecting traditional notion), to 'productivity' (reflecting resources provider's concerns) and 'quality' (reflecting taxpayers' concerns). The notion of performance, therefore, becomes more multi-dimensional in this form of PMS. The PMS of Swedish Tax Authority can be seen as an example here.

Between the two extremes (at point B), labelled 'Behaviour', are located the tax authorities which define organisational performance primarily in terms of revenue collection but add a few behaviour related PIs as well. The concerns of resources provider may also be included by measuring 'efficiency' or 'productivity'. The case of HMCE before 1998 is a good example here. The targets and measures are all in terms of clearly identifiable outputs like revenue collection, productivity and charter standards.

The categorisation proposed in Fig 5.2 will be helpful in locating the position of HMCE after various rounds of accounting changes that were introduced during the period of analysis of this PhD research.

## **5.2 Accountability for Performance in HMCE**

In the previous chapter the historical origins of HMCE established that it had a past which was deep rooted in law enforcement. This has arguably defined and shaped the ethos of the organisation. It is therefore not surprising to find references to this ethos in the discourse and traditional accountability system of the organisation. For instance, one interviewee referred to this risk management role in day to day operations:

“..... all SMEs will be under my area but obviously we would look at them we would break those down for our own purposes into the larger ones that the officers might visit; the very small ones which maybe some of the more junior officers might visit etc; and *it's on the basis of risk, on the basis of amount of tax which is actually at risk....*” (MM1: p 3)

Another manager refers to this risk management role as the deciding factor for allocation of staff:

“Yes; the numbers will change, because the numbers of officers that we get are allocated to us in each region is based on the risk; the department would negotiate with the Treasury for a certain number of staff to actually allocate them to the regions as they need it to best address the risk” (MM1: p 4).

An NAO report also refers to the risk management role of HMCE in the wake of possibilities of fraud and evasion.

“... All taxes are subject to the risk of fraud and evasion, including smuggling. Given the need to balance countermeasures with the need for goods to flow freely, total prevention is not realistic and some loss is inevitable. There are no reliable estimates of the total level of loss from outward diversion fraud. Nevertheless, to tackle fraud, Customs seek to allocate their resources based on broad assessments of the risks” (NAO, 2002b: p 1)



Prior to the accounting changes introduced by the New Labour government in 1998, HMCE reported its organisational performance as a part of *Next Steps* Report<sup>52</sup>. The report helps in understanding the traditional form of performance reporting reflecting the law enforcement ethos of the organisation. For instance in the *Next Steps Annual Report, 1997* the opening statement of the Chancellor of Exchequer is as follows:

“Customs and Excise's annual Management by Outputs agreement with me supports the move towards a more strategic overview of its main functions. The Department's performance in meeting the agreed targets is monitored in-year and reported in subsequent agreements. The agreement develops annually as part of the Resource Management programme, keeping pace with the improved information on costs, activities and outputs that will become available” (Next Steps Report, 1997a)

It clearly refers to accountability for performance through monitoring of the outputs based targets. The emphasis upon revenue collection based output targets is evident from the following description of performance of HMCE in the same report.

“In 1996-97 Customs and Excise achieved or exceeded almost every operational target for collecting the due amount of tax and duty and, in doing so, collected net receipts of £82.4 billion. This represents 43% of central government taxation and an increase of 4.9%, in real terms, on receipts for the previous year. The Department also exceeded its target for the prevention of the importation of drugs” (ibid)

In addition to revenue collection, productivity (or efficiency) is cited as another indicator of performance in the report:

“The cost of each £1 of tax collected was 0.1p for excise duties, 0.7p for VAT, rising to 7.7p for customers duties (though much of that expenditure arises from non-revenue regulation of imports and exports). This generally compares favourably with the figures for 1995/96, with an improvement in the cost of collecting VAT and a small increase in the cost of collecting customs duties” (ibid)

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<sup>52</sup> As explained in Chapter 4, by *Next Steps* initiative in Thatcher's era agencies were created which acted independently but reported their performance to the parent ministry

The exhaustive list of performance indicators in the Next Steps report, 1997 contained 78 targets belonging to 12 categories. The outputs targets represented almost all spheres of activities that came under the control of the department (see Annex 5.2).

No	Category	No of targets
1	UK Revenue	1
2	VAT, APD, IPT and Landfill Tax	2
3	VAT, IPT and Landfill Tax	1
4	VAT and IPT	2
5	VAT	13
6	EXCISE	12
7	VAT, IPT and Excise –customer service	1
8	Protection of society	12
9	Imports	12
10	Facilitation	7
11	Trade Statistics	11
12	Overseas Activity	4

Table 5.1: Measures/PIs appearing in the *Next Steps* report  
(Tabulated by the PhD author from Next Steps Report, 1997b)

If the targets are categorised they can be presented in the following way:

No	Measures Category	% of total measures
1	Revenue collection and compliance measures	61
2	Good Behaviour related measures	13
3	Operational/HR/ Efficiency related measures	7
4	Other measures	19

Table 5.2: Categories of measures listed in Next Steps Report, 1997  
(Tabulated by PhD author from Next Steps Report, 1997b)

It can be seen that while the greatest bulk of measures remained traditional revenue collection and law enforcement related, we do notice inclusion of measures which can be classified as non-traditional. However all the PIs and targets are outputs-based which are easy to define and report. Therefore, in terms



of the categorisation proposed earlier in the chapter, the performance reporting of HMCE can be positioned near point B i.e. 'behaviour'. In this type of PMS, there is some information regarding 'behaviour' aspect of performance, however, the traditional dimension of revenue collection retains its superior place in the hierarchy of these measures. For instance, the opening paragraph about the performance of HMCE in the *Next Steps* Report, 1998 bears the signature and photo of Gordon Brown. It can be seen that the emphasis on traditional targets of performance has not changed in this report:

"In 1997/98 Customs and Excise achieved or exceeded 90 per cent of its targets. These covered the whole range of the department's operational activities, including UK revenue collection, deterrence and detection of smuggling of prohibited goods, ensuring compliance with international customs obligations and supply of trade statistics. The department collected 42% of central government taxation, equating to net receipts of £90.1 billion. The cost of collecting each £1 of revenue was 0.1p for excise duties, 0.6p for VAT and 8.8p for customs duties. These costs represent an overall improvement with the cost of collecting excise duties remaining static, VAT collection falling and that for customs duties rising slightly (largely as a result of continuing reductions in tariff rates)" (Next Steps, 1998).

### **5.3 Conclusion**

In the preceding sections a framework for classifying PMSs in the context of tax authorities was developed. With the help of actual examples of how performance is measured and reported in three different countries, a three point categorisation was proposed. It ranged from traditional to outcomes based PMS. The PMS of HMCE, prior to implementation of accounting changes by the New Labour government, was then positioned on this categorisation by examining the then PIs used. The empirical analysis of the measures/PIs established that accountability for performance was mostly traditional, but some emphasis upon good behaviour was also noticeable. It was, therefore, concluded that HMCE's traditional accountability is for revenue collection where a few additional

dimensions of performance (efficiency and Charter standards) were also included. The PMS of HMCE before 1998 was therefore positioned on point B of the proposed categorisation. But NPM inspired reforms do not advocate mere ‘*accountigisation*’. What it stresses most is that accounting should flow out of a clearly defined outcomes-based strategy and thus should play the role of a strategic tool of change management. For instance, Osborne and Plastrik (1997) caution that:

“We have not listed performance measurement as an approach because we do not believe that the act of measuring itself has enough power to force fundamental change in most public organisations. It is a critical *competence* organisations need if they are to use the consequences strategy...But some public organisations have measured performance for years, with virtually no impact” [p. 132, their emphasis.]

So it can be concluded that the traditional form of performance measurement and reporting as reflected by *The Next Steps Reports* did not qualify the NPM’s desired use of accounting. Therefore, the accounting changes introduced by the New Labour government were applied to HMCE in order to bring about a fundamental change in the ethos of the organisation. In the next chapter the changes are examined critically to find out their desired effect and what actually happened to the ethos of the organisation.



## Chapter 6

### **The Environmental Pressures and HMCE**

#### **Introduction**

In this chapter the external environment of HMCE is reviewed because institutional theorists (e.g. Powell and DiMaggio, 1991) believe that often organisational changes are implemented due to various pressures emanating from the external environment. The external environment of HMCE is made up of various components. Being a Governmental department it is affected by the policies of the central Government. Being a tax administration, it is also affected by the discourse about best practices adopted by other taxation regimes and promoted by world bodies like IMF, OECD etc. Therefore, in the next sections these external environmental factors are analysed.

#### **6.1 The Norms Setting Environment**

From time immemorial monarchs have used tax revenues to run government, fight wars and pay for their own lavish lifestyles. They were, by and large, not accountable for the manner in which money was used. For instance, an account sheet on display in the HMCE National Museum, Liverpool shows *Nell Gwyn*, the king's mistress, receiving a regular income from the Crown. However, it is equally true that taxation has remained one of the most contentious issues in the human history. With the renaissance in Europe many influential authors started

writing about the features of a good tax system<sup>53</sup>. Adam Smith's celebrated maxims of taxation are still regarded as the canons of a good tax system. In chapter 2 Book 5 of *Wealth of Nations*, he advocates that taxes should be:

- *Equitable*, i.e. the taxpayers should contribute in proportion to their respective interests.
- *Certain*, i.e. the tax liability should not be worked out in an arbitrary manner.
- *Convenient*, i.e. it should not be cumbersome for the taxpayers to pay their taxes
- *Economical*, i.e. should not result in high administrative and/or compliance costs.

Despite prolific writings of many authors on taxation with roots in political science and economics, Cook (1952: p 627)'s observation is still valid:

“For some 600 years mankind through some of its ablest minds, has sought to solve the problems of raising these funds in the most effective and least painful manner, but none of the methods devised has been able to disguise the fact that the money has to come out of somebody's earnings, directly or indirectly.”

This reality may account for two important and overriding concerns with regards to desirable virtues of a tax system nowadays. First, there is a greater emphasis upon outcomes or results for the money sent on public services. Osborne and Gaebler (1992), who are considered to be the proponents of NPM, base their work on the premise that the taxpayers had become more assertive about how the

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<sup>53</sup> Groves (1974) classifies such authors into four schools of thought. First, the rationalists (e.g. Adam Smith and J. S. Mill) consider ethical ends important and advocate the ability to pay as measured by income as one of the most primary concerns of a tax system. Second, the opportunists (e.g. John Ramsay McCulloch and Galbraith) consider administrative efficiency as the most important concern and advocate the famous metaphor “most feathers for least squawking”. Third, the direct expenditure proponents (e.g. Fisher and Kaldor) extol encouragement of saving as the fundamental virtue of a good tax system. Fourth, the *functional* school proponents (e.g. Henry George and John Hobson) call for a tax system that would not affect production but targets windfall income.



tax revenue was spent (p 20). Thus, *value for money* is an important consideration in new public financial management. The second concern is about trust building by respecting taxpayers' rights<sup>54</sup>. Daunton (2001) argues that lack of trust in any relationship results in non compliance and increases the need for greater compliance enforcement<sup>55</sup>.

The tax authorities all over the world also seem to be paying heed to the importance of trust building as the foundation of tax policy. For instance, Williams (2001) states that the *Australian Tax Office* is moving away from a purely deterrent regulatory framework towards a graduated suite of responses that are tailored to compliance behaviour. Similarly the Secretary of the *Commonwealth Institute of Taxation*, U.K who was interviewed by this PhD researcher termed *self-assessment* as the defining feature of tax policy during the last decade or so. The PhD research compared the contents of speeches made by the three heads of tax authorities of Canada, Australia and UK at different forums and found some striking similarities. All the three tax authorities underwent reforms and reorganisation and achieving goodwill of the taxpayers was considered to be the driving force behind all reform initiatives<sup>56</sup>. The tax heads

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<sup>54</sup> Through a working papers series, the Centre for Tax System Integrity of Australian National University, Canberra emphasises the importance of taxpayers' perceptions about the ways in which they define their relationship with institutions and, more specifically, how they align themselves with social policy (e.g. Braithwaite et al., 2001).

<sup>55</sup> Daunton (2001) mentions three tiers of trust based relationships in a 'fiscal state', (i.e., the modern state which can raise revenue by taxation or borrowing). First, does the taxpayer trust other taxpayers to pay for public action? Second, whether the state was using funds for the intended purpose and revenue was not wasted? Third, can the state trust taxpayers to make their payments?

<sup>56</sup> For instance, the head of Australian Tax Office (ATO) says:

"..... Equally, adoption of a self-assessment system reflects the reality that effective tax administration is not about collecting every last dollar payable under our tax laws; it is about optimising collections under those laws in a way that instils community confidence that the system is operating properly" ATO (2002).

also mention the supporting role of accounting information in the reforms process. The UK and Canadian heads refer to the '*Balanced Scorecard*' while the Australian chief refers to the Taxpayers' Charter standards. These are important evidences of NPM inspired change initiatives where accounting is considered to be an important tool for reforming public sector management around customer needs.

There is no recorded academic research on using performance measurement for accountability in tax authorities. However the OECD carried out a review of the performance measurement practices in its member countries. This report has its limitations as it only refers to OECD countries and thus a generic classification of tax authorities can not be induced. The report (OECD, 2002) however is informative as to how performance measures are used in the OECD countries. In the report performance measures are classified into three groups: first, measures that relate output to input i.e. *productivity*; second, measures of *quality* and *taxpayer satisfaction*; and, third, measures of outcome with respect to revenue and compliance i.e. *effectiveness*. The main *input* measures identified by the survey are cost and labour (expressed in work hours).<sup>57</sup> Typical *output* measures

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Same concern for image management is noticeable in the speech of Canadian counterpart:

“While our name will change, as will many of our internal functions, our value system will remain intact - fairness, integrity, professionalism, respect, cooperation, and customer service” (CCRA, 2000).

The head of Inland Revenue, U.K strikes almost similar notes as he terms customer service as the most important attribute of reforms:

“With these challenges has come the growing recognition that the function of the Inland Revenue must be to enable as well to regulate..... It means laying a greater emphasis on making it as easy as possible for taxpayers, whether companies or individuals, to understand what they owe us by way of tax and to pay it” (IR, 2002).

<sup>57</sup> In some countries such reports cover all activities, in others only specific areas, e.g. audits. The purpose is to attribute input (measured as work hours or direct labour cost) to different activities,



were found to be related to the workload (number of taxpayers or tax returns) or to tax control (number of audits or verifications).<sup>58</sup> It can be seen that the ‘outputs’ are derivatives of revenue collection figures. Therefore, in terms of the proposed categorisation of PMS of tax authorities in chapter 5, these would lie close to the ‘traditional’ form where the revenue collection figures themselves are reported as outputs.

The OECD study found that *productivity development* is reported regularly by most tax authorities. *Productivity* is the ratio between output and input, depending upon the distinction between output and outcome. Output is normally expressed in physical terms, while input can be expressed either as costs or as work hours.<sup>59</sup> There are fewer standard practices reported in OECD countries for the evaluation of outcomes. Given that the OECD *input-action-output-outcome* model places great emphasis on outcome recognition and evaluation as essential to the effectiveness, and therefore performance, of tax authorities, the paucity of research on practices in this area of performance measurement is significant.

Three aspects of *quality* measurement are identified by the report. First, quality can be measured in terms of *timeliness*, like average processing time for applications. Second, quality can be identified with respect to *legality* and *professional* standards, which can be assessed by inspections or review of selected files. Third, quality can be expressed in terms of client satisfaction,

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functions, processes, programmes or outputs. This information can also be used to apportion overhead cost to the appropriate offices or functions.

<sup>58</sup> Some countries were found to include taxpayer contacts in the form of telephone enquiries and visits to tax offices in their output measures. Most countries also seem to regard revenue, at least additional revenue recovered by audits, as output although it can also be regarded as outcome.

<sup>59</sup> There is a variety of productivity measures depending on different definitions of output. A common measure is cost per taxpayer. When revenue is included in output, productivity is typically expressed as administration costs as a percentage of total revenue.

which can be studied by taxpayer surveys. Most tax authorities carry out such surveys and some do so regularly. There are many other ways to get feedback from clients: for example focus groups, exit surveys, letterboxes for suggestions and complaints etc. Some countries measure quality against published standards also known as taxpayers' charters.

According to the OECD report, all tax authorities measure and report collected revenue, which, when set as a target, is an important aspect of performance for tax authorities. Much attention is also focused on the direct revenue effects of tax control, and in several countries audit programmes are expected to achieve certain targets in terms of additional tax revenue. Moreover, it is also common practice to relate additional revenue to direct costs to get a measure of audit efficiency. The main function of tax control, however, is to prevent and deter tax evasion. In some countries attempts have been made to measure the deterrent effect of tax control.

The OECD report suggests that overall *effectiveness* of the tax system can be expressed as the ratio between actual tax revenue and the theoretically correct yield - the difference between the two being commonly referred to as the *tax gap*. Several tax authorities have reported to be involved in studies of the black economy. However, it is contended by the report that generally, such studies have not been found to provide much practical guidance as no tax administration in the survey reported to carry out such studies regularly.

## **6.2 Political Environment**

HMCE is a central government department and has to follow and implement the policy instruments of the government. The *New Labour* Government announced



its public sector reform agenda through a white paper *Modernising Government*.

As is clear from the foreword of Minister of Cabinet, the document is the basis of the public sector reforms initiated by the Government:

“Modernising Government is an important statement for the Government. It is a programme of reform for the future. And it is a series of new measures which the Government will implement now” (Cabinet Office, 1999b: p 5).

Three aims are cited by the white paper as central to the modernising agenda:

- Ensuring that policy making is more joined up and strategic.
- Making sure that public service users, not providers, are the focus, by matching services more closely to people’s lives.
- Delivering public services that are high quality and efficient.

The language used by the strategy paper clearly reflects the ideals of NPM. Terms like ‘customer focus’, ‘quality’ and ‘efficiency’ are very closely associated with the NPM literature.

The NPM literature advocates making *customer focus* ideal of the private sector the cornerstone of the public sector reforms (e.g. Araujo, 2001: p 617). The phrase *customer focus* has become an important element of faith in the official publications of the new Labour government as well. This is also clear from the increased proportional usage of the term *customer* in the annual and spring reports of HMCE for the last two years. A textual analysis of the four documents presented in Table 6.1 supports this observation:

	HMCE 2002 spring report	HMCE 2002 annual report	HMCE 2003 spring report	HMCE 2003 annual report
Word or phrase	Hits	Hits	Hits	Hits
Total words count	9,601	52,357	13,076	60,740
Customer	25	25	28	61

Table 6.1: Usage of the phrase ‘customer’ in HMCE reports

Not surprisingly *customer-focused* ‘accounting’ features prominently in the performance reporting of HMCE after 1998.

The official document which articulates what ‘*customer focus*’ means for the New Labour Government was produced by Lynton Barker, a senior consultant of PricewaterhouseCoopers who was contracted by *Public Services Productivity Panel* of the PM office for the said purpose. The aim of the publication as stated by the Chief Secretary to the Treasury in his foreword is to take “*a new look at customer focus, in particular the need to radically shift the whole of an organisation – strategy, policy and front line delivery - to face its customers*” (Barker, 2001: p 1)<sup>60</sup>.

If *customer focus* is about refocusing service delivery around the needs of the recipients of public services then the need for measuring *success* in satisfying customers is understandably important. In the private sector clients/customers surveys are carried out regularly for feedback purpose. To imitate the same, in 1998, the Cabinet Office’s *Modernising Public Social Services Group* commissioned MORI, the market research company, and Birmingham University's *School of Public Policy* to set up a *People's Panel* which was made

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<sup>60</sup> The document articulates what ‘customer-focused’ government means and what is required to focus, at organisational as well as individual level, on the public as the ultimate customer. Recognising the debate on choice of words for recipients of goods/services, the writer of the report contends that ‘customer’ is preferable because ‘citizen’ is too focused on political identity and ‘stakeholder’ is not always seen to include ordinary members of the public. The publication emphasises that “*Customer Focus*” in the public sector is about refocusing services around the needs of the citizen as a customer of public services, rather than the problems of those who provide the services. It signifies an organisational culture that aims to address the needs, expectations and behaviours of the public, and then adjusts every aspect of the organisation to align with customer values. This includes the entire delivery chain from policy-making through to front-line services - including strategy, organisational design, business processes, performance measures, information systems and support processes.



up of 5,000 members of the public. It had a profile that was representative of the

WHAT DOES CUSTOMER-FOCUSED GOVERNMENT LOOK LIKE?

Overall	
<ul style="list-style-type: none"><li>■ Clearer, outward focus and vision for public servants and their Ministers</li><li>■ Deeper, shared understanding of main customers</li><li>■ Information is organised by customer groups, across government where required</li><li>■ Higher stakeholder satisfaction</li><li>■ What is measured and rewarded is driven by what customers value</li><li>■ Better alignment of resources to objectives</li><li>■ Different staff motivation and improved morale</li></ul>	
Policy	Service delivery
<ul style="list-style-type: none"><li>■ Proactive, outward driven policy processes with high stakeholder and public engagement</li><li>■ Clear approach to defining the 'public interest' in terms of customer needs</li><li>■ Ministers are involved in structured process of customer identification and management</li><li>■ Ministers and officials at all levels seek to foster a team approach to understanding and meeting customer needs</li><li>■ Staff have particular relationship management and/or customer representative roles</li><li>■ Promotion is based on new values and skills</li><li>■ Risk management focused on customer values and concerns</li><li>■ Closely managed partnerships and exchanges with external organisations</li><li>■ Policies that are more likely to be workable and achieve their objectives</li></ul>	<ul style="list-style-type: none"><li>■ Services are designed and delivered around customer needs and interests</li><li>■ Common definition and information about customer segments is shared across organisations from policy to delivery</li><li>■ Effective channel strategy (management of different methods of communicating and transacting with customers, e.g. telephone, web, paper, face-to-face)</li><li>■ Policy teams use abstracted operational data from delivery systems</li><li>■ IT and e-government projects are embedded in wider transformational projects which address people, processes and performance management</li><li>■ Large IT projects achieve measurable gains in effectiveness</li></ul>

Fig 6.1: Official elaboration of customer-focused government (Source: Barker, 2001: p 6)

UK population in terms of age, gender, region and a wide range of other demographic indicators. MORI recruited the Panel from a random sample of addresses across the UK between June and September 1998. The system came to an end in January 2002, after three satisfaction surveys were conducted (wave 1 1998; wave 5, 2000 and wave 6, 2002) of the members of the panels.

In order to implement the *customer focus* ideal in service delivery the Government initiated many changes. Along with many structural reforms like electronic delivery and Private Finance Initiative (PFI), the Government also



used accounting changes for implementing its agenda. It is this aspect of reforms which is of interest to the PhD study. In fact the belief that accounting information is an effective change management tool (Miller, 1990) is deep-rooted in official rhetoric. For instance, the HM Treasury issued a special publication, jointly authored with the Cabinet Office, National Audit Office, Audit Commission, and Office for National Statistics which aims to guide the central departments, HMCE inclusive, in implementation of the accounting changes as part of the overall change agenda of the Government. The key official publication uses the acronym of FABRIC to lay down the essential characteristics of a good PMS:

- Focused on the organisation's aims and objectives,
- Appropriate from all stakeholders' perspectives,
- Balanced in terms of coverage of all work areas,
- Robust so that it can withstand any changes and not depend on any particular staff members,
- Integrated into organisation's business activities and not as a standalone data compilation activity, and
- Cost effective (HM Treasury, 2001a: p3)

The publication stresses the need for maximising the gains in performance as against the cost of implementing a PMS (p 16). It is further stressed that the measures should avoid any perverse consequences, and that they should be relevant, attributable in terms of accountability, well defined, timely, reliable, comparable and verifiable (p 17).

Reflecting the influence of Balanced Scorecard, the publication lays down the strategic planning framework with performance measurement having a pivotal role in it (p: 6). The model prescribed by HM Treasury places organisational



objectives at the top, giving rise to carefully thought-out performance measures and targets. It is stressed that the measures and targets should be owned by the employees, so that they feel accountable for their performance. The performance review is also stated not to be a standalone process but must be rigorous enough to act as reinforcement for provision of targeted service.

The same pivotal role of performance measurement is evident in the “Cascading Planning in the Public Sector” model (ibid: 7). Patterned on the model of Lynch and Cross (1991), this is also shaped like a pyramid:

- *Strategic Priorities*, e.g. PSAs and local PSAs rest on the top.
- The next layer of the pyramid is of *More Detailed Aims and Objectives*, e.g. SDAs, Best Value Performance Plans, and agency targets.
- Next is *The Organisation’s Strategy*, e.g. business plans for government departments.
- Then comes the *Business Group Plans*, being internal plans and performance measures/standards.
- The bottom most layer is that of *Individual Staff Performance and Accountability Plans* including staff performance development and performance appraisal.

An NAO publication (2001) also gives a central role to performance measurement in identifying key stages for strategic public sector policy making. In the circular framework the performance measures are not only embedded in the strategic objectives but they also help refine the objectives themselves through monitoring and evaluation of results. The publication explains with the help of a diagram how 3Es model is to be applied in the U.K. The model is somewhat similar to that of Pollitt and Bouckaert (2000), referred to in the previous chapter and is based upon the *inputs-process-outputs-outcomes*

framework. ‘Inputs’ are defined as the resources that contribute to production and delivery such as labour, physical assets, and IT systems. ‘Outputs’ are defined as the final products, or goods and services produced by the organisation for delivery to the customer. ‘Outcomes’ are defined as the impact or consequences for the community, of the activities of the government.<sup>61</sup>

Economy, efficiency and effectiveness represent the desired relationships between inputs, outputs and outcomes. An economy measure looks at the costs of acquiring the inputs to the programme. An efficiency measure looks at whether we are getting the maximum output for the inputs that go into the process. Finally an effectiveness measure looks at whether the outputs of the programme lead to the desired outcomes.<sup>62</sup> The overall framework is plotted in Figure 6.2.

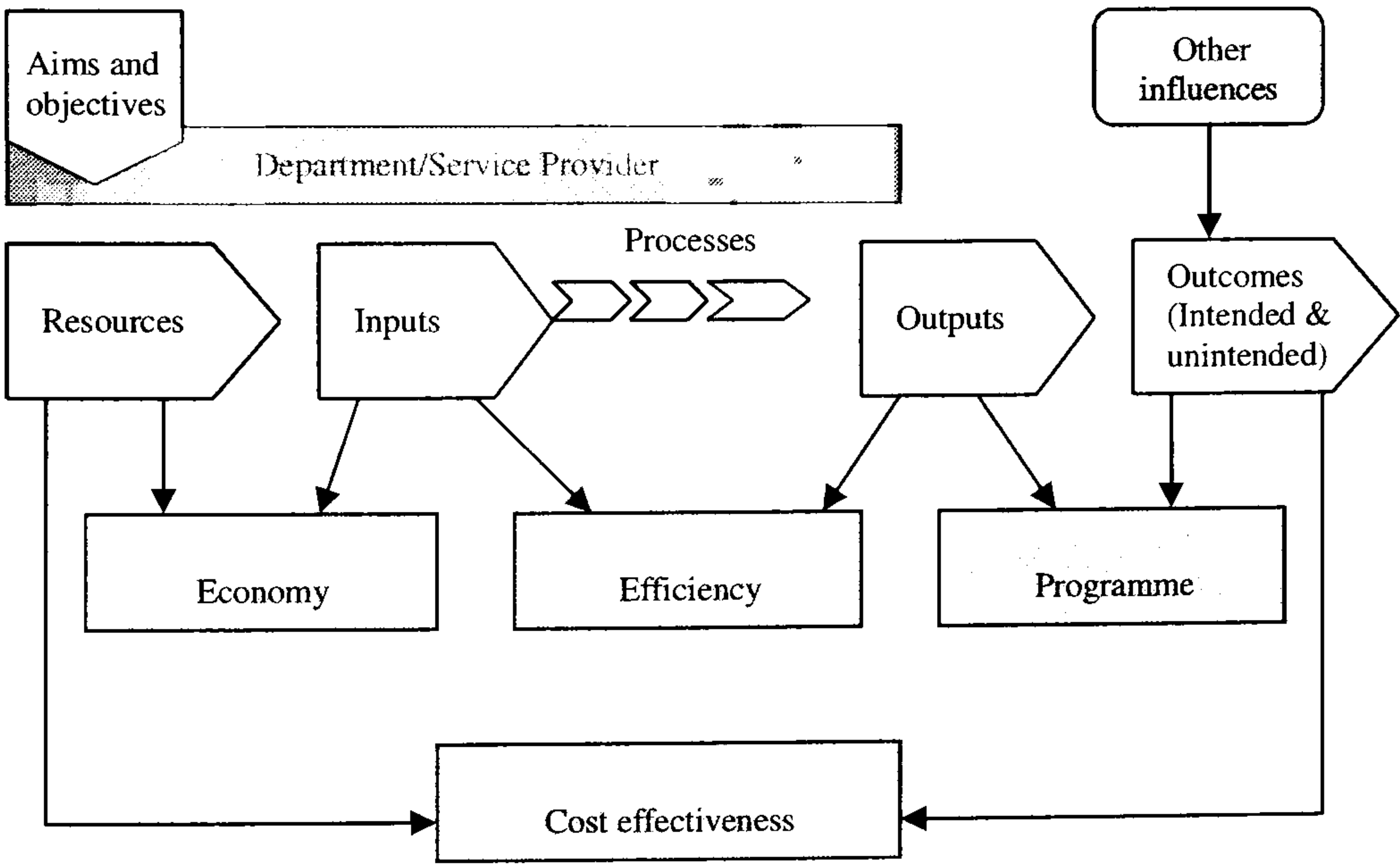


Figure 6.2: Relationship between Inputs, Outputs, and Outcomes (NAO, 2001: 2)

<sup>61</sup> For example, in an NHS context “outputs” might be the number of effective medical treatments, or operations of the appropriate quality which take place in a hospital. In contrast, “outcomes” might be longer life expectancy and better health. A complete list of definitions provided by the NAO publication is appended as Annexure 6.1

<sup>62</sup> Again in an NHS context, an economy measure might look at the costs of acquiring drugs for a certain treatment. An efficiency measure might consider the relationship between given hospital facilities and standards of care, and how many patients are being treated. An effectiveness measure might consider estimates of the number of people giving up smoking because of an anti-smoking campaign, as an indication of the effectiveness of that campaign in improving people’s health.



Value for Money (VFM) or 'cost effectiveness' relates money resources to the final outcomes, while the *Other influences* on the final outcomes represent the factors which are beyond control of the organisation.

### **6.3 The Accounting Changes**

The New Labour Government conducted a thorough review of departmental aims and objectives and a zero-based analysis of each spending programme to find the best way of delivering the Government's objectives. The Government's assessment of the economic and budgetary position for a medium-term of three year was concluded in July 1998 and was termed *Comprehensive Spending Review* (CSR). HM Treasury (2000a: 1998b) claims that the CSR forced the departments to take a more fundamental look at the effectiveness of spending, rather than just bidding for extra resources every year; to find cross-departmental solutions to achieving its objectives and to encourage joint working and that it allowed spending to be directed towards the Government's key objectives

The CSR 1998 was followed by another Spending Review in 2000.<sup>63</sup> The two reviews are linked by the HM Treasury (2000b) as:

- The 1998 Comprehensive Spending Review (CSR) set firm three-year public spending plans 'from scratch' for the first time ever and introduced a new spending control regime
- The 2000 Spending Review rolls forward the CSR plans, refines the control system and uses a new accruals budgeting system

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<sup>63</sup> HM Treasury (2000a: p7) contains the following introduction of SR 2000: "The 2000 Spending Review, together with the Economic and Fiscal Strategy Report and Financial Statement and Budget Report contain the Government's assessment of the medium-term economic and budgetary position. They set out the government's tax and spending plans, including those for public investment, in the context of its overall approach to social, economic and environmental objectives. They will form the basis of submissions to the European Commission under Article 99 (ex Article 103) and Article 104 (ex Article 104c) of the Treaty establishing the European Union".

As a result of these spending reviews two changes are very important in terms of NPM's advocacy for a more strategic place for accounting tools. First, the *Resource Accounting and Budgeting* (RAB) and second, the *Public Services Agreement* (PSA). The RAB process can be traced back to the 1993 Budget speech of the then Chancellor of the Exchequer.<sup>64</sup> A White Paper in 1995 (HM Treasury, 1995a) announced that budgeting would indeed be on the RAB basis from the year 2000. According to the new system Parliament has to give approval for central government expenditure not on *Estimates* basis but rather on *resource-based Estimates*. Similarly the departments are also required to report its performance on RAB basis. i.e. from *Appropriation accounts* to *resource accounts*. Two important implications can be identified. First, while the *Appropriation accounts* were cash accounting based the *Resource accounts* follow the accrual basis and are more on the pattern of private sectors published accounts. Second, utilisation of resources is accounted for in terms of organisational objectives. The public sector organisation has to seek financial resources from the parliament by referring to organisational objectives the organisation desires to meet.

The second important accounting change is the outcomes based PSA framework of performance measurement and reporting. The New Labour Government has in fact operationalised the public sector PM models cited in policy publications through the instrument of PSA. The PSA is complemented by *Service Delivery Agreement* (SDA). Each PSA sets out the aim of the department or programme, the supporting objectives and the related performance targets showing what will

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<sup>64</sup> A Green (discussion) Paper (HM Treasury, 1994a) announced that the first RAB based reporting would be for the year 1998–99. It also announced that the first published set of accounts would be in 1999–2000 after which discussions would take place to see whether budgeting could move to a new basis.



be delivered. The accompanying *SDAs* set out how each PSA will be delivered together with key output targets that are critical to the delivery of the PSA outcome targets. They cover issues such as the quality of service, the development of new processes and progress towards general objectives such as those relating to ethnicity, procurement and the prevention of fraud. Another accompanying document *Technical Notes* provides more precise details of how targets are to be measured. They explain exactly what is being measured and clarify terms and data definitions used in the published PSAs (NAO, 2001).<sup>65</sup>

According to the Government PSAs are the vehicles of change, as is evident from a speech delivered by the *Chief Secretary to the Treasury*:

“.... The 1998 Comprehensive Spending Review PSAs were a revolution in this respect. And for our departments, I think they were something of a revelation too. PSAs challenged them for the first time to think about what were the outcomes they really wanted in each policy area.....

... To conclude, I believe PSAs have been something of a revolution. Departments have recognised the real benefits for their own management of clear priorities and targets, and we will see further steps forward in the quality and clarity of the PSAs which come out of this spending review” (Treasury, 2000c).

*The Treasury* monitors departments’ performance against their individual PSA targets and provide quarterly reports to the Ministerial Committee on Public Services and Public Expenditure. The Committee periodically examines the progress that individual departments have made towards achieving their targets. Performance against PSA targets is made public in departmental reports.

It is claimed that PSAs and SDAs are designed to promote joined-up Government as they not only focus on the achievement of targeted outcomes

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<sup>65</sup> The PSAs for 2001-04, published in July 2000, were fewer in number than those produced following the Comprehensive Spending Review in 1998. The Agreements covered the 17 main government departments, four cross-cutting programmes, local government and the Northern Ireland Office. The PSAs were again refined in 2002, with greater emphasis on fewer outcomes.

under the responsibility of a given department or group but also enable the contribution of other departments and their priorities to be recognised and co-ordinated in support of high-level objectives (NAO, 2001). Figure 6.3 illustrates how PSAs and SDAs complement each other.

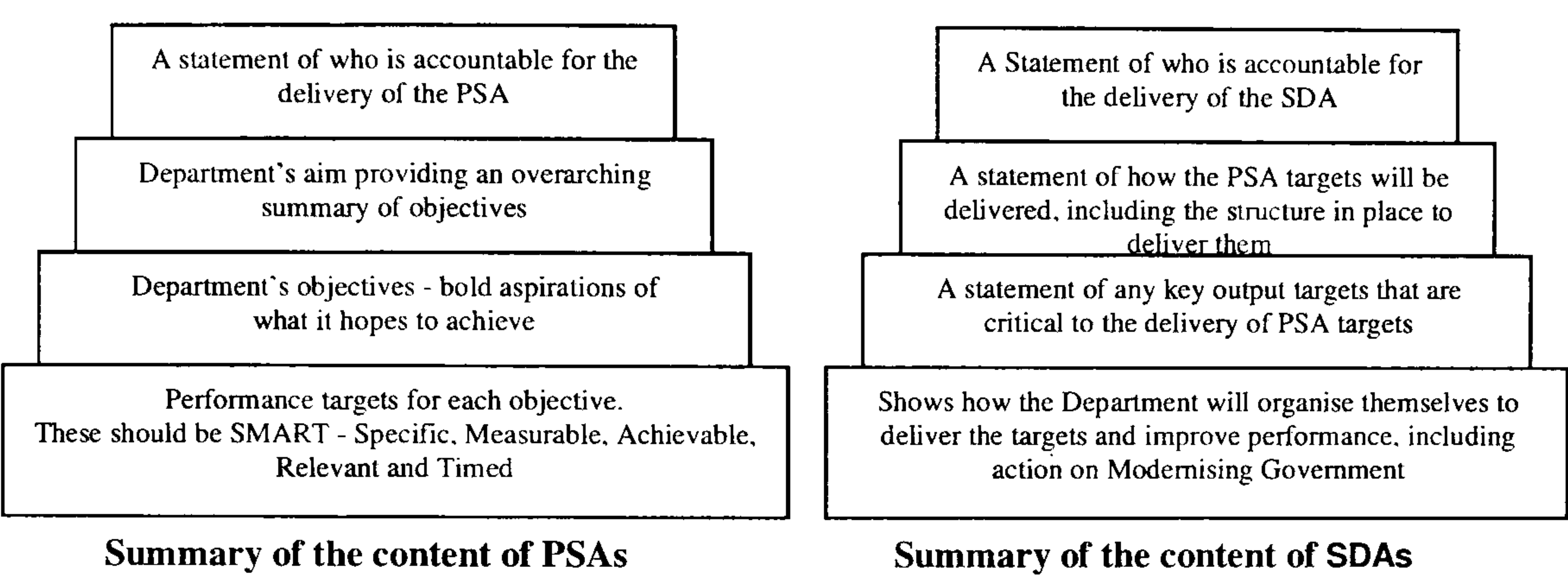


Figure 6.3: Comparison of PSA and SDA content (NAO, 2001: p 14-15)

### 6.4 Conclusion

In the previous chapter the notion of performance in tax administration was theorised as a categorisation ranging from traditional to outcomes based PMSs. A review of the norm setting environment in this chapter established that there has been a growing emphasis upon better customer-focus and productivity gains and that there was a shift towards outcomes based performance management in the OECD countries. The review of official publications establishes that the aforementioned norms are also reflected by the new approaches towards public sector management in the U.K. Accounting has received significantly important role, as evidenced by the formal implementation of PSA framework. Since HMCE has to follow and implement official guidelines, it logically follows that the department’s accountability and PMS would exhibit these features. In terms



of institutional theory, the governmental prescription of PSA based accountability system would generate coercive pressure upon HMCE to change its PMS.

In Chapter 2 reference was made to the works of NIS authors (e.g. Powell and DiMaggio, 1991). They argued that organisational reforms are often caused by normative, mimetic and coercive pressures emanating from the external environment. The review of norm-setting and political environment surrounding HMCE suggests that owing to these pressures HMCE should move towards the NPM inspired multi-dimensional outcomes based PMS. In the next chapters further evidence is examined to ascertain the extent of the NPM styled strategic shift and the role of accounting in facilitating it.

## **Chapter 7**

### **Breaking the Tradition - Accounting Changes in HMCE**

#### **Introduction**

In this chapter the accounting changes introduced by HMCE after the New Labour government came to power are reviewed. These accounting changes were implemented in order to realize the PSA based strategic shift. A significant feature of the analysis is to notice the importance of context when accounting changes are used as a vehicle of change.

#### **7.1 HMCE and Organisational Reforms**

The restructuring of HMCE along functional lines was discussed in detail in chapter 4. Being one of the oldest public sector organisations, HMCE has seen many waves of reforms. A detailed description of such changes is outside the scope of this study. However many governmental reforms have affected the organisational structure and working of HMCE. For instance the five year Fundamental Expenditure Review that began in 1994 required “restructuring”, “delaying”, “staff cuts” and “cultural change” (Colville and Packman, 1996). It had its main thrust upon high risk, complex areas of Customs work rather than on routine, low risk areas. It was viewed as an opportunity to undertake a wide scale review of departmental activities to find the most effective way of providing services, involving moving resources away from compliant traders to the riskier end of the trader population. Similarly, local VAT offices were given more



authority to manage work in their area in the light of their judgment of local circumstances (Simpson and French, 1998; Hansford, 1997).

Two official publications set the stage for implementation of accounting changes in the late 1990s. A White Paper (HM Treasury, 1998b) followed by an earlier publication (HM Treasury, 1998a) published new objectives for government departments along with measurable targets in the form of PSAs for all the departments. The foreword to the White paper is from the Prime Minister Tony Blair and sets the tone of the reforms:

“Too often in the past, governments have only made commitments for what they put into public services – money, manpower and policies – not for what the public will get out in return. That is what really matters. People rightly expect modern services that work well, meet real needs, and use public money fairly and efficiently. That is why PSAs set out each department’s aims and objectives and then show how much progress we expect to make and over what timescale, through concrete targets” (HM Treasury, 1998b: foreword)

The shift to customer-focus is quite evident. The publication explains how each department would achieve the desired objectives.

The second key document published in March 1999 by HM Treasury is titled “The Government’s Measures of Success: Output and Performance Analyses”. The publication (HM Treasury, 1999a: p 2) proudly claims that the OPAs “*complete the picture by showing the indicators which will be used to measure and monitor success against those objectives and PSA targets*. The publication terms OPAs as *the basis* for performance reporting to the public. Admitting that OPA was still work in progress, the publication lays down the basic structure of OPA as:

- the department’s objectives;
- the PSA targets for each objective;

- the indicators for measuring progress against the objectives and targets and outturn against them;
- performance against the PSA productivity targets to demonstrate the efficiency of the organisation (ibid: p 2).

The publication also contains the OPA of HMCE (p 103-109) and comprises two parts (Annex 7.1). Part 1 lists down six organisational objectives, the underlying policy targets and the quantitative targets to assess performance against those policy targets. Part 2 lists productivity related targets which continue to be the essential part of performance reporting since the Thatcher era.

The first objective in OPA is:

**Objective 1: To secure the UK revenue yield from indirect taxes while minimising costs to businesses, as a key component of the Government's policy of ensuring sound public finances.**

If the Part 1 objectives are closely analysed one fact becomes quite noticeable. The traditional emphasis on revenue collection and fraud detection retains its supremacy in the new scheme of performance reporting. Under this objective two policy targets appear. The first reads:

“The Department will collect each year amount of forecast UK Revenue yield from indirect taxes, subject to external factors outside the Department's control. The actual amount will be agreed annually with the Minister by April each year” (PSA target i).

The OPA declares two measures of success for this dimension of performance.

First, *the Revenue receipts* and second, *% monthly arrears of the 12 month trader liability*. Therefore, actual revenue collection figures and debt



management figures appear as the two most important quantitative measures of performance.

The second policy target is given the heading of 'Fraud'. It reads:

"The department will agree targets for UK revenue evasion prevented by April each year, which will cover the prevention of civil and criminal fraud in both VAT and Excise.

By 31 March 2002 the Department will achieve an increase of at least £80 million in the revenue value of detected alcohol and tobacco fraud, including from smuggling. This will be measured against the baseline of £76 million revenue value of excise goods detections in 1997-98. (PSA target ii)

These policy targets are to be assessed with the PIs of "*Total UK Revenue evasion prevented*", "*Revenue value of detected alcohol and tobacco fraud and smuggling*", "*Number of major excise smuggling organisations disrupted or dismantled*".

These measures of performance are also closely identifiable to the traditional notion of performance of HMCE.

The second objective relates to anti-drugs and other contrabands smuggling operations. The policy targets and PIs also pertain to reducing availability of drugs in the U.K market and disruption of drugs smuggling organisations.

Up to objective 2, it is a very traditional form of performance measurement and reporting. However with objective 3 there comes a break from the past. Even though the objective itself sounds quite traditional:

**Objective 3: To secure compliance with statutory, EU and international customs obligations in ways which facilitate global trade and help the single**

**market work thereby supporting the Government's aim to make the UK an attractive place to do business.**

However one of the underlying performance targets clearly intends to usher in the NPM inspired customer-focus ideal into the performance reporting of HMCE. The following policy target requires *a 6% improvement in customer satisfaction*:

“The Department aims to go on improving its customer service performance in key areas which will be the principal focus of its modernisation programme. The Department's performance against this target will be measured by surveys at the start and end of each CSR period. By the end of the CSR period, the Department will aim to have achieved increased satisfaction of 6% in the areas of VAT, customs freight and excise, which are to benefit from the investment under the modernisation programme” (PSA target iv).

The remaining objectives 4-6 deal with ancillary duties of the department like provision of trade statistics, assisting tax regimes of other countries and providing policy advice to the government. The long list of productivity targets under part 2 aims to improve customer service while ensuring reduction in costs. These include measures like national call centre besides other cost saving measures.

The OPA framework is the first attempt on the part of the government to use accounting changes as a policy tool to implement the notion of *accountability to the customers* as the basis of the performance measurement and reporting. Since it was a public sector wide change, HMCE was also obliged to adopt the change. It is worth noting here that the customers-related targets were also present in the Next Steps form of reporting of HMCE. But what is different here is that customer-focus is measured directly in terms of customers' responses and not simply in the form of outputs. It can be noted that part 1 not only includes



traditional measures of performance but it also includes an explicit measure of customers' satisfaction as one of the strategic PIs. If the government is considered a trustee of taxpayers' money, the part 2 measures of performance on productivity dimension also reflect a concern for the customers' welfare. In terms of 3E model of public sector accountability (i.e. *economy, efficiency and effectiveness*) it refers to the concern for *Value for Money* accountability of HMCE. So it can be concluded that the OPA based PSA framework in 1998 is a significant step towards aligning customer focus based accountability relations along with the traditional system of accountability and performance reporting. Likiermann (2000) represents the positivist views on accounting changes by discussing the concerns on implementation of RAB and OPA and concludes affirmatively:

“The commentary for output and performance indicators is one example of this. Such information will provide those who give informed comment outside, including Parliamentary Select Committees, the opportunity to question the figures and the basis on which they are used” (p 259).

However, the move towards a new framework of performance reporting was not a very smooth one. The difficulties with regards to HMCE's PMS will be analysed in the next chapter, when OPA was finally subsumed into PSA 2000. However, even at a general public sector level, the potential difficulties were even recognised by the reformers themselves. For instance, the OPA document admits work in progress nature of the reforms:

“Today's publication therefore shows work in progress. But it is an important milestone which allows the public to see the shape of future reporting and gives them the opportunity to comment on the work done so far” (HM Treasury, 1999a: p 2).

Talbot (1998: 4) criticises the fact that OPA was announced to be a separate document and not made a part of the *Resource Accounts* as per the original proposal. He attributes this decision to the fact that government department managers (e.g. chairpersons of tax authorities and permanent secretaries of central government departments) did not like their departmental performance to be scrutinised as the NAO would audit the *Resource accounts*. In a written memorandum to the Select Committee on Treasury Professor Talbot emphasises this point again:

“There has been a deliberate decision to exclude Departmental performance information from audit (hence the separation between the Departmental Annual Report and Accounts and the OPA). The reason advanced is that performance measurement at this level (Departments) and of this type (outcomes) is sufficiently novel that audit would expose this delicate flower to unwarranted external castigation when the inevitable problems arise.

On the other hand, the Comptroller and Auditor General apparently wants the NAO to audit both Departmental and other performance information (from Agencies, NDPBs, etc.) routinely”. (TSC, 1999a)

In a supplementary memorandum to the same committee, Talbot makes two specific recommendations. First, he stresses the need for dropping the label of output performance and analyses<sup>66</sup> and argues that:

“... it be replaced by the term "Public Service Agreement—Annual Report". The detailed content of the document should then be brought fully into line with the content of the PSAs. It would remain an Annual Report, but incorporating cumulative data” (TSC, 1999b)

The second recommendation is about audit of Departmental Public Service Agreement Annual Reports by the National Audit Office.<sup>67</sup>

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<sup>66</sup> Two reasons are cited for that in the memorandum. First, the terminology of ‘Output and Performance Analysis’ is incompatible with either the content of the actual OPAs or the new emphasis on outcomes. Second, having a separate set of documents not clearly linked to PSAs seems somewhat anomalous and can potentially generate confusion.

<sup>67</sup> It appears from the format of PSAs after SR2000 that while the terminology of OPA was dropped as per Professor Talbot’s recommendation, the audit of PSA by NAO is still a grey area.



## **7.2 Towards Outcomes Based PMS**

In year 2000, the Government published new PSAs for its departments under *Spending Review* in 2000 (SR 2000). The HMCE, in its CSR (1998) PSA, had six objectives, seventeen PSA targets and 46 performance indicators. In the new PSA (Annexure 7.2) HMCE had now fewer aims and key performance measures than the first PSA discussed in the previous section. The Department's new PSA which ran from 1st April 2001 for three years had now three objectives and eight key performance targets, though the actual number of total performance indicators against all the performance targets increased to 62. According to the department (HMCE, 2001a) the reorganisation of the department along functional lines was necessitated by the demands imposed by the new set of challenging outcomes based targets of PSA 2001-2004. The 2001 Spring Report of HMCE emphasises the importance of the new PSA:

“The SR2000 PSA represents a major change for the Department, with a new overall aim and a sharper focus, as the targets are focussed on outcomes rather than outputs” (HMCE, 2001b: p10)

This marked reduction in key performance areas was welcomed by the then HMCE Chairman, Richard Broadbent, in a testimony before the Treasury Select Committee (TSC):

“At a strategic level, if an organisation is trying to do more than really a handful of things ... it is going to fall over itself” (TSC, 2000b: para 52).

The TSC, however, remained sceptical and thought that “*the problem of too many targets, of uncertain rationale and status, has not yet been fully dealt with*” (ibid).

Despite this marked scepticism by the TSC members, the PSA 2000 was path breaking in three main ways. First, it was based fully on the notion of ‘outcomes’ instead of ‘outputs’. Second, the departmental expenditure (resources) was to be reported according to key performance targets of the PSAs. So now being part of the *Resource Accounts* they could be discussed and examined by the parliamentary committees. Third and most important from HMCE’s context is the formal attempt to relegate the traditional form of accountability and performance reporting and instead give greater prominence to the customer focus based accountability relationship. This will be further examined in section 7.

With PSA 2000, the Government finally embraced outcome based measurement as the basis of PMS for the public sector organisations. Talbot (2000) analyses the move from outputs to outcomes measurement and argues that initially the terminology (e.g. outputs, intermediate outputs etc) was derived from formal economics. The shift to ‘*outcomes*’ as the basis of performance measurement is, according to the author, a shift from formal economics definitions to those of public policy traditions.

Together with this broad policy shift towards social/public policy based PMS, the refinement work of performance measurement and reporting also resulted in more explanatory documents in 2000. The PSAs of all department were now accompanied by *Service Delivery Agreements* (SDAs) and *Technical Notes*. The SDAs were published on 3 November 2000, and set out how each PSA would be



delivered together with key output targets that were critical to the delivery of the PSA outcome targets. Taking forward the *Modernising Government* agenda of the Government, these additional documents supported the PSAs and showed how departments would improve performance and how performance would be measured.

It was noted in Chapter 6 that the PMS of HMCE is shaped by the high level strategic management policies of the central government which are spelt out in a number of policy documents. The influence of Lynch and Cross (1991) in such official publications was found to be quite evident. This pyramid like approach to performance measurement is evident in the design of SR (2000) PSA of HMCE as well, as shown in Fig 7.1.

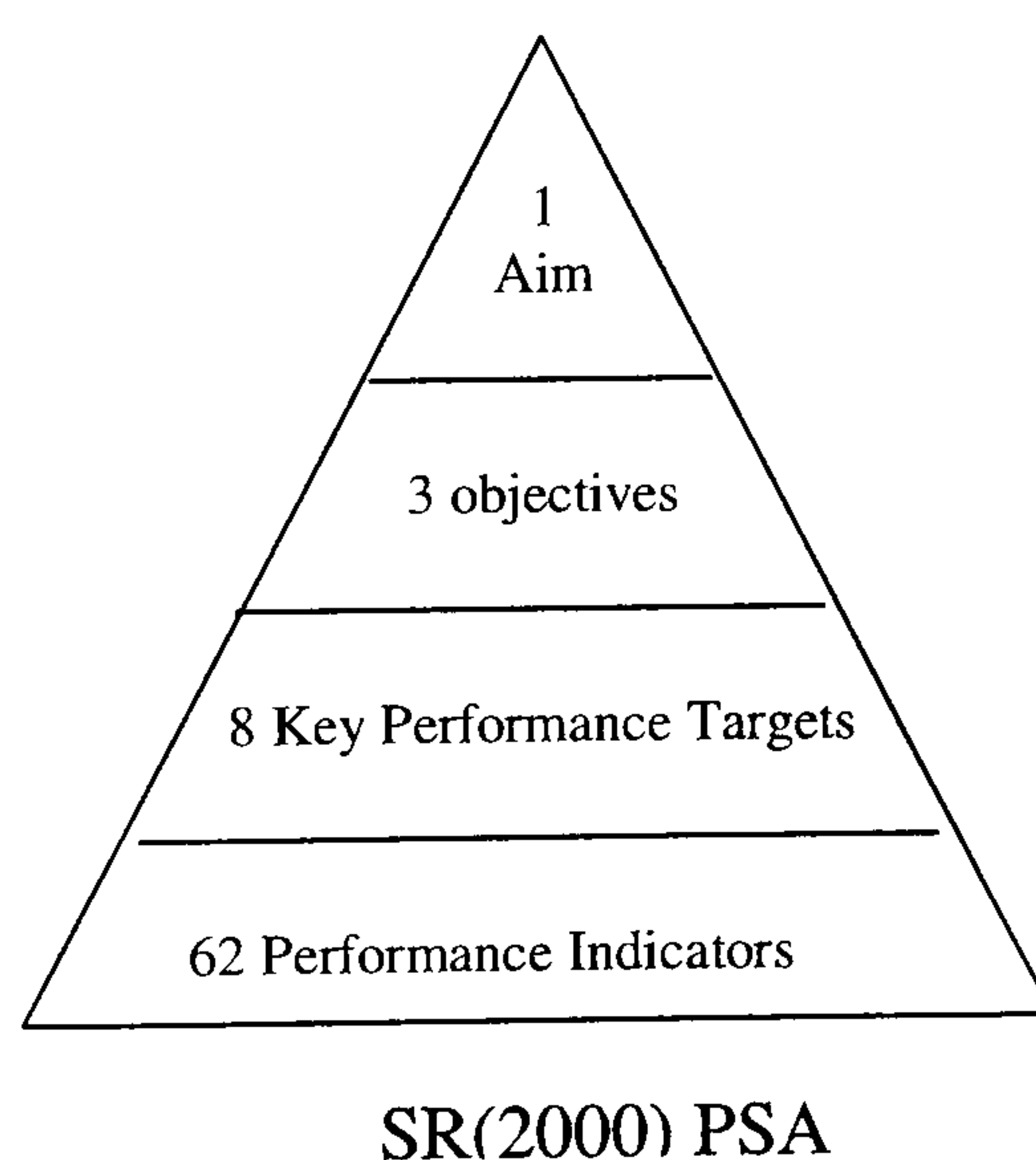


Fig 7.1: The pyramid design of PSA of HMCE (figure developed by the PhD author)

The over-arching “aim” of HMCE is: “to administer the indirect tax and customs control systems fairly and efficiently, and make it as easy as possible for individuals and businesses to understand and comply with their obligations”

(HMCE, 2002b: p18). The three objectives of the Department have been outlined as:

- “To collect the right revenue at the right time from indirect taxes”.
- “To reduce crime and drug dependency by detecting and deterring the smuggling of illegal drugs and other prohibited and restricted goods”.
- “To reduce the costs of international trade and improve the level of compliance with customs and statistical requirements” (ibid.).

When the management team responsible for performance measurement of VAT in HMCE was asked to comment upon the relationship between policy level and operational level performance measurement, the written official reply (EM1) distinguished between PSA measures and operational level measures, where the former were said to be outcome based and cross-functional, reflecting the key aims of the Department. According to the reply, the operational level measures were more likely to be output based (although not always) and were linked to the PSA outcomes.

The reply further informs that the PSA is broken down to:

- high level business indicators that reflect the work of the function i.e. VAT business and show whether we are on track to achieving PSA outcome; and
- operational measures, which look at aims, objectives and activities of each operational area, and link them to indicators and PSA target. We decide on the best way to measure their effectiveness/success, and set realistic, stretching targets using business experts and relevant data sources (ibid).

## **7.2 The PSA 2000**

The PSA 2000 is in the form of policy targets with specific quantitative targets.

Given below is a brief description of the targets that were part of the PSA.



Targets 1 and 2 of the HMCE PSA are to deliver year on year improvements in the compliance of businesses with their obligations, and to reverse the current trend in tobacco smuggling (so that by 2004/05 smuggled cigarettes represent no more than 18% of the market).<sup>68</sup> (see Annex 8.1 for estimates of tax fraud). These targets come under the first objective of collecting *the right revenue at the right time* from indirect taxes. Four key indicators for measuring improvement in compliance have been specified, each of which is to be measured separately with individual targets for each one of them. The indicators correspond to the key areas of compliance like *registration; right tax at right time; assessments/voluntary disclosure*; and the use of *special schemes* (HMCE, 2002c).<sup>69</sup>

Target 3 of reducing the availability of Class A drugs by 25% by 2005 and by 50% by 2008 specifically addresses the second objective of reducing crime and drug dependency by detecting and deterring the smuggling of illegal drugs and other prohibited and restricted goods. ‘Availability’ is defined as the amount of Class A drugs available for distribution to the general population in the UK. This

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<sup>68</sup> The market share of smuggled cigarettes is the percentage of the total amount of cigarettes consumed that is made up of smuggled cigarettes. This is measured using an internal statistical model (HMCE, 2002c).

<sup>69</sup> Baseline data for the timeliness of payments and declarations/returns and on trader debt was made available from existing internal systems from April 2001. HMCE had been developing the Compliance Testing Programme (CTP), to capture data on the accuracy of traders’ declarations/returns. Through the CTP, information on numbers, values and type of error including both under and overpayments is gathered, via compliance questionnaires, from a statistically valid number of assurance audits. Once the information is collected it is analysed and assessed by the Department’s statisticians and analysts who are independent of the business areas. Progress is reported on a quarterly basis (ibid).

in turn is dependent on the Department's successful disruption activity like seizures at entry and distribution points.<sup>70</sup>

Targets 4-8 come under objective number III which calls for reducing the costs of international trade and improving the level of compliance with customs and statistical requirements. The implied assumption behind this objective is that compliance can be improved if the taxpayers are provided with more efficient and customer focussed service. Target 4 aims at improving the level of compliance in connection with imports and exports. That also includes *Intrastat*, the collection of statistics on the movement of goods between member states within the European Community. Improvements are indicated by percentage improvements in the accuracy of frontier import and export declarations, fulfilling inland customs requirements and the timeliness of *Intrastat* declarations.<sup>71</sup>

Dealing categorically with improved provision of services, target 5 calls for electronic provision of 100% services by 2005 with at least 50% uptake by the users, target 6 calls for continued reductions in the businesses' compliance costs, target 7 requires achieving average annual productivity gains of at least 2.5% per year until 31 March 2004, without detriment to accuracy or customer satisfaction, and target 8 calls for achieving a 6% improvement in customer service from the 1999 baseline, as measured by the annual Customer Service Index (CSI), by April 2002. The CSI represents responses to a combination of *Overall Satisfaction* and *Service Factors* as asked in the Business Needs Survey

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<sup>70</sup> Internal data capture systems were made available to record the weight of drugs seized; however, seizure data also came from the National Crime Squad and Home Office.

<sup>71</sup> The information is derived from internal systems and the CTP.



1999. In addition to *Overall Satisfaction*, the factors enquired about are: *communicates effectively; provides consistent service; understands commercial pressures on business; treats me fairly; and takes business needs into account.*<sup>72</sup>

Table 7.2 below partially reproduces a four column table of performance outturns from the *Spring Report*, 2002. Column 1 lists the PSA outcome based target. The corresponding indicators for measuring this outcome are listed in column 2. The actual numerical target and quarterly performance against this target are listed in column 3 and 4 respectively (see Annexure 7.2 for full details).

PSA Target	Performance Indicator	Target Out-turn	Quarter 3 Out-turn
1. Deliver year on year improvements in the level of compliance of businesses with their obligations.	A percentage increase in the number of declarations/returns made on time.	88%	87.08%
	An increase in the value of payments made on time.	90.20%	90.22%
	An improvement in the accuracy of declarations/returns submitted. (Measured using CSI results from the Compliance Testing Programme.)	79.7	84.1
	A reduction in the value of trader debt as a percentage of liability.	1.41%	1.88%

Table 7.2: PSA Target Evaluation (HMCE, 2002d: p 16)

**7.3 An Appraisal of SR (2000) PSA**

In the earlier section three important changes with respect to SR (2000) PSA were identified. Of these the third one needs special mention. It relates to shifting emphasis to customer-focus based accountability from the traditional revenue collection and law enforcement based performance reporting. In chapter 4, the ethos of HMCE was identified as law enforcement defined. This conclusion is

<sup>72</sup> The Business Needs Surveys are carried out by external research companies.

not the result of personal judgement of this PhD author alone. In fact a TSC report refers to the law enforcement culture based ethos of the department:

“Our key conclusion concerns the law enforcement culture which pervades all aspects of the work of Customs and Excise and which we argue must be altered in order for compliance costs to be minimised” (TSC, 2000c: para 88).

When the then chairperson of the department claims that the department did give importance to *customer focus*, the TSC very unequivocally replied:

“Dame Valerie Strachan's assertions that there are several discrete cultures within Customs and Excise and that "people in our advice centres do not look or sound like law enforcers" seem to us to underestimate the extent to which a common, underlying culture, based on the department's historical law enforcement traditions, pervades all aspects of the department's work. The considerable body of evidence we received complaining of the law enforcement culture of Customs and Excise, and the negative impacts this culture has on compliance, is too powerful to be dismissed. The law enforcement culture of customs work should not influence the collection of tax revenue from businesses” (ibid; para 133).

A joke shared by a VAT consultant during an hour long interview with this PhD author is also an apt description of how the outsiders viewed the ethos of HMCE:

“On a joint exercise by the Inland Revenue and Customs & Excise, investigating a tax case, they undertake a dawn raid on the premises of various taxpayers. Whilst waiting to enter the premises, the Inland Revenue Inspectors are sitting in their van discussing with their legal advisers what powers they have, what papers they can seize, who they can interview, etc. In another van, Customs & Excise officers are polishing their sledge-hammer!” (EM7).

In view of the afore-mentioned examples it can be argued that the reorientation of the department along the NPM inspired *customer focus* would require basic transformation of the ethos of the organisation. The SR (2000) PSA can therefore be seen as a bold attempt on the part of reformers to transform the culture of HMCE with the help of accounting changes. This can further be analysed by examining the performance reporting under the new arrangements.

The HMCE produces two reports about its organisational performance. The first one is of preliminary nature, called *Spring Report*, while the other is the final and



more detailed one and is called *Annual Report and Accounts*. With the implementation of RAB in 2001-02, like other departments, HMCE also started presenting *resource accounts* in its performance reports. What is important to notice is that the traditional measures of performance, i.e. revenue collection figures, are no longer in the PSA key performance measures. They are even not included anywhere in the resource accounts. Instead they are reported separately as a *Trust statement*. This relegation implies that revenue collection is considered not as a *key performance measure* but just as a *trustee function* of HMCE.

It is important to note that while the traditional accountability (i.e. holding taxpayers to account) fails to get prominence in the new PSA based measures, the NPM inspired customer-focus based accountability has specific measures such as *Customer Satisfaction Index* (CSI) which required 6% improvement in taxpayers' satisfaction with HMCE's performance. Therefore, SR (2000) can be seen as a very bold and determined effort on the part of governmental reformers to use accounting changes to redefine dimensions of performance in HMCE. Whether such accounting changes transformed the ethos of the organisation? How did the organisation react to such changes enforced from the top? These questions need examination of further evidence which is presented in the remaining part of this section and will be carried through to the next chapters as well.

Obtaining access to the head of a Government department like HMCE is not a realistic possibility for a PhD student. However the oral evidence he gave before the TSC members provided the PhD author with rich textual data for analysis purpose. The tensions the new framework of measuring performance under

SR(2000) PSA created for HMCE's top management are very clear from the conversation that took place in one of the hearings. For instance when the chairman of the department was asked as to why the desired level of improvement in customer satisfaction was not achieved, the chairman replied that:

“... I think one of the things we are learning is the provision of service is not necessarily quite the same as satisfaction, and I sometimes ask myself whether, in a sense, taxpayers can be satisfied, if you like, by our providing more services. We have dealt with this target and I am sensitive to that .... I am probably personally coming to the conclusion that we will not do that by going on providing service innovations. We are going to have to get to grips with something much more fundamental ...” (TSC, 2002: para 42).

The frustration of the chairman with measuring customer focus through the measure of taxpayers' satisfaction is quite evident as he questions if taxpayers can ever be satisfied. Thus in the department's view the tax-payers satisfaction (measured by *Customer Satisfaction Index*, CSI) was a measure which was not in line with its traditional measures of performance. In the private sector customers' satisfaction is assumed to be a function of better service delivery. The chairman of HMCE distinguishes the tax department from service delivery organisations by expressing his doubts on the presumed causal link between taxpayers' satisfaction and improved service delivery. The department is declared not to have come to grips with this new measure of performance which places the department in an accountable position directly to the taxpayers. The Chairman makes an apologetic defence by claiming that the CSI measure did not reflect all the changes that had been introduced in the area of service provision. In the same oral evidence he argues that better customer satisfaction might be achieved by



concentrating upon the changes linked to e-technology and IT, which would transform the nature of the interaction of the taxpayers with the tax department.

In response to this apologetic defence the chairman was asked by the TSC members if he would consider changing the target in the future. The Chairman replied:

“... [W]e can go back, if you like, to output measurements which is easy. It was actually our idea, saying, “Let us go for an outcome, let us go for satisfaction”, and we are learning now that it is quite difficult to measure, so I think we will try to replace it, but I would like to keep pushing to see if we can keep an outcome base rather than just going back to outputs, which are sort of Mickey Mouse, really” (ibid: para 43).

It can be seen that the department was not very happy with using the outcomes based target for *service delivery*. The Chairman admits that measuring performance in terms of customer satisfaction is difficult in the context of tax administration.

Another important measure of performance, productivity (or efficiency) was not entirely new however its measurement was based more on *outcomes* instead of traditional *outputs*. The measure is not directly customers related and reflects more the concern of Government as the funds provider. But since the funds come from the taxpayers’ money so in a way the Government acts as a trustee and ensures on behalf of taxpayers that the HMCE uses all funds in the most effective way. So the measure can be viewed as indirectly customer related.

The target for productivity gains in SR (2000) PSA was to achieve 2.5% increase. However the outturn was bizarre, – 8.9 %, which was noted by the TSC

members and the Chairman of HMCE was asked to explain this negative score on this important dimension of performance.

In reply the Chairman once again puts up a very apologetic defence by attributing the reason of poor performance to the outcomes based measurement of productivity. He argued that if the traditional measures of activity (e.g. the unit costs of collecting tax, tax collection and law enforcement activities) were considered the productivity would have been positive. He further elaborated that out of 60 PSA related performance indicators, only seven were included for productivity measurement; of which only five were paper-counting measures, like “Did you get the returns in?” The following excerpt from the oral evidence of the Chairman before TSC illustrates very clearly the department’s frustration with outcomes based targets:

“We got the target wrong. This again was an attempt to try and create an outcome based target, and I do not want to labour the point, but I think it is sometimes underestimated how different an outcome target is from an output target, how difficult to construct and how difficult to get an organisation to meet. ... So they have led me to look very carefully into why this target has this rather interesting result. The answer is this: that attempt to create an outcome target is calculated by taking only a small number of our PSA measures - because not all of them are very easily translated into outputs” (ibid: 44).

The departments’ problems with the outcomes based targets and measures did not end with the *taxpayers’ satisfaction* and *productivity*. Another key measure of performance related to *debt management*. The poor performance on that dimension, the Chairman clarified, was caused by good performance on law enforcement dimension. The department had been successful in detecting missing trader fraud which led to a big increase in debt figures. The Chairman



terms the negative results on new measures of performance an illustration of “complexity” of outcome targets and call for carefulness in interpreting them.

#### **7.4 Conclusion**

In this chapter the important changes introduced by SR 2000 PSA in the performance measurement and reporting regime of HMCE were reviewed. It was found that with this spending review a complete shift from ‘outputs’ to ‘outcomes’ took place. More importantly, the NPM inspired customer-focused accounting changes relegated the traditional measures of performance in terms of law enforcement and revenue collection to secondary importance (i.e. in the form of Trust Statement) while the customer-focus based outcomes measures of PSA acquired primary importance. This resulted in tensions between the traditional form of PMS and the new customer-focused PMS. The empirical analysis of the measures used during the period of analysis helps in proposing a framework for analysing accountability relationships and PMS which will be discussed in the next chapter.

## Chapter 8

### **Theorising Accountability Relations in a Tax Administration**

#### **Introduction**

In the previous two chapters the performance measurement of HMCE before and after the NPM inspired accounting changes were analysed. It was not surprising to find that the traditional PMS of an old organisation like HMCE reflected the law enforcement ethos of the organisation. It was noted that the SR (2000) PSA sought bringing about changes in the ethos of HMCE by giving greater prominence to customer-focused measures of performance. The tension created by these top down imposed changes was evident from the confessions made by the Chairperson of HMCE before the members of TSC. Earlier in chapter 2 a simplified accountability framework for public sector organisations was proposed. Analysing the evidence of performance measurement discussed in chapters 6-7 with insights from principal agent model of accountability, stakeholder theory and structuration theory a framework of accountability relations for tax authorities is developed in this chapter. Based on the notion of *reciprocity* of accountability the framework is built around the competing notions of traditional accountability in HMCE and the NPM inspired theme of customer-focused accountability. The framework helps in conceptualising a shift in emphasis from one form of accountability to another through accounting reforms.



## **8.1 The Building Blocks**

Fowles (1993: 102) states that ‘accountability’ has become a widely used word in discussions of public policy, both as “a buzzword or simply as an emblem”. However the notion of accountability is still considered to be quite complex (Robinson, 2003) and authors keep proposing theories and frameworks to understand the notion in both private and public sectors. For instance Roberts and Scapens (1985) elaborate a theoretical framework for analysing the operation of systems of accountability within organisations. Ahrens and Chapman (2002) use structuration theory of Giddens (1984) to examine the accountability system of a restaurant chain. Gray and Jenkins (1993) argue that the analysis of accountability in the public sector had remained focused upon ministerial accountability due to the dominance of political science in the field of public administration. They stress the need for a conceptual framework of accountability which draws on other social sciences but takes as its focus the accountability relationship itself. They propose a framework based on principal agent model. Referring to the work of Bird (1973), they state that stewards are given resources by the principal, where stewards expect a reward for their services while the principal expects that the resources will be used according to the aims and objectives set by the principal. The authors argue that in addition to stewards and principal the third element of an accountability relationship is ‘code of accountability’. They define it as “a system of signals, meanings and customs which binds the principal and steward in the establishment, execution and adjudication of their relationship” (p 55).

Roberts (2001) reviews the works of other authors and identify various mechanisms of accountability such as formal and informal types of

accountability. The author terms procedure-based accountability, direction-based accountability and performance based accountability together as the *administrative model* of accountability.

The existing literature is focused on identifying and classifying various forms of accountability relationships. Theorising the interaction of various accountability relationships in a situation where the principal and agent can have reciprocal roles is not so well addressed in the literature. This PhD study provided an opportunity to fill this gap and in the remaining part of the chapter the framework based on reciprocal accountability relationships will be developed.

In chapter 3 the main research question was decomposed into four constituent questions with the help of principal agent model of accountability. The questions were:

1. Who is (are) the principal (principals) in the case of a tax administration?
2. Who is (are) the Agent (agents) in the case of a tax administration?
3. What is the format of accounts and what are its contents for the purpose of performance measurement and reporting?
4. What are the remedial/control powers available to the principals?

Questions 3 and 4 can be seen as approximating to the *code of accountability* as defined by Gray and Jenkins (1993). The framework can be improved if insights are drawn from the stakeholder theory which provides the following set of questions (Frooman, 1999):

1. Who are the stakeholders?
2. What do they want?



3. What influence strategies do they have?
4. How are they going to use those strategies?

If the principal agent model related schematic questions and the stakeholder theory related questions are considered together, the following questions can provide a framework for analysing accountability system of a public sector organisation.

1. Who are the stakeholders?
2. How are they related to one another in terms of principal agent model?
3. What does the principal want from the agent(s)?
4. What is the format of accounts and what are its contents for the purpose of performance measurement and reporting? To what degree do the accounts reflect the demands of the principal?
5. What influence strategies does the principal have to ensure that the accounts reflect his/her expectations?
6. What are the remedial/control powers available to the principal if he/she is not satisfied with the level of performance reported by the agent(s)?

In the NPM inspired literature and official publications the term ‘accountability’ is repeatedly used. In chapter 2 it was noticed that accountability relationships can be of various forms such as public, managerial or legal accountability. Since accountability for the purpose of this PhD research was defined in its formal meaning of ‘giving and taking of accounts’, it is important to know who is giving accounts to whom and in what format?

The stakeholders in the case of HMCE are restricted to only those who have a relationship of ‘giving and taking of accounts’ on a regular basis. As such the following can be identified as the main stakeholders:<sup>73</sup>

- Taxpayers<sup>74</sup>
- Government (*The Treasury* is the department to which HMCE is accountable)
- HMCE (the department can be seen as comprising *the Board* which formulates policy in consultation with the Treasury and *the tax collectors (operational level employees)* who interact with the VAT registered businesses on a regular basis)

In the simplified accountability model proposed in Chapter 2, three stakeholders were identified as *Government*, *Public Sector Organisation* and *Citizens*. In the context of HMCE, the taxpayers take the place of citizens. At a broader level, i.e. in terms of public/political accountability, the taxpayers are also citizens, so they enjoy the rights which citizens enjoy in any democratic society. However, when legal accountability is considered, the taxpayers are individuals acting on their own, with the assumption that they are motivated by a desire to minimise their tax liability. The citizens, as a whole, want every tax payer to pay the correct amount of tax. In order to achieve this goal the tax collectors are equipped with necessary legal powers to hold tax payers to account for their tax liability.

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<sup>73</sup> The importance of other stakeholders like the society and media is well recognised however they have not been considered here since they are not directly involved in ‘giving and taking of accounts’ in a formal manner or on a regular basis.

<sup>74</sup> VAT registered Businesses are assumed to be the *taxpayers* for HMCE. Technically the VAT registered businesses are not the taxpayers as VAT is a tax on final consumers but since these businesses collect and deposit VAT on behalf of the government, they have a ‘giving and taking of accounts’ relationship.



The taxation organisation is also seen to be characterised by a dual role. In one role, it holds the taxpayers to account by making them file tax returns and then audit those returns. In the second role, it is held to account by the parliamentary committees for its conduct towards the taxpayers (in their capacity as citizens). The department can, therefore, be seen as comprising two stakeholders for the purpose of accountability framework. One, the Board; which is responsible for policy formulation, and whose chairperson regularly appears before the parliamentary committees to account for organisational policies towards the taxpaying citizens. Second, operational level tax collectors who interact regularly with the taxpayers and hold the taxpayers to account with their legal powers. This understanding helps in answering the question as to what kinds of accountability relationships these stakeholders have with each other. The guiding premise is that the stakeholder who gives accounts for performance is ‘the agent’ while the stakeholder who demands and receives accounts is the ‘principal’. Accountability is the cementing relationship for the *principal agent* model where the principal allows the agent to continue utilising resources due to the accountability powers of *incapacitation* and *deterrence*<sup>75</sup> which the principal enjoys. In the case of HMCE different kinds of ‘*accounts taking*’ can be identified.

The traditional job of operational level employees of HMCE is to audit the accounts of taxpayers (i.e. VAT registered businesses) on a regular basis. This relationship makes the VAT officers and their managers the *principal* and the taxpayers who (in their individual capacity) present their accounts (in the form of

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<sup>75</sup> These terms were explained in chapter 2 with reference to principal agent model of accountability.

VAT tax returns and other accounting records) for audit as the *agent* in terms of principal agent model. This form of accountability relationship can be labelled as **‘legal accountability relationship’**. Since the tax collectors are the operational arms of the Board and Government, the two also stand included in this form of accountability relationship.

The operational level employees report their performance on a regular basis to the Management Committee of *the Board*. So this account taking makes *the Board* the *principal* and the operational level employees the *agent*. The form of this accountability relationship can be labelled as **‘managerial accountability relationship’**. The Board of HMCE reports the overall organisational performance to the Government (the Treasury). This relationship of account taking makes the Board the *agent* and the Government the *principal*. The form of this accountability relationship is also a **‘managerial accountability relationship’**.

The Government (the Treasury) presents its performance report to the parliamentary committees which audit these reports with the help of experts in the field and NAO. In this relationship the parliamentary committees can be thought as acting on behalf of taxpayers (as citizens) and thus are the *principal* while the Government can be termed the *agent*. This form of accountability can be labelled as **‘public/political accountability relationship’**. The tax collectors and the Board are the operational arms of the government so they also stand accountable to the taxpayers in this relationship. They are also accountable for behavioural aspects of performance and the quality of services provided to the taxpayers.



This duality in the role of tax payers and tax collectors results in an accountability relationship which is of 'reciprocal' nature. According to structuration theory expounded by Giddens (1979: 1984) all social systems are comprised of day-to-day social interactions involving situated activities of human agents existing in time-space, and are constituted by regular, reproduced relations of interdependence between either individual agents or a collective group (1979, p. 69). Giddens uses the term 'integration' which is defined as "regularised ties, interchanges or reciprocity of practices between actors or collectivities" and refers to the degree of interdependence of action (or "systemness") associated with system reproduction (1984, p. 76). The notion of 'reciprocity' is important for the accountability system of HMCE as an element of reciprocity can be identified in the process of '*accounts giving and taking*' in the case of HMCE.

It is not being suggested that this reciprocity is only unique to tax authorities as some degree of reciprocity is present in all social relationships. However, as stated at the very outset in Chapter 2, only formal form of accountability is considered for this PhD research. A relationship qualifies as an accountability relationship only if it is characterised by a regular and formal 'giving and taking of accounts'. Based on this qualification, the public sector organisations can be categorized on a continuum of *reciprocal accountability relationship* which is defined as a relationship in which two actors are accountable to one another by virtue of mutual accountability expectations.

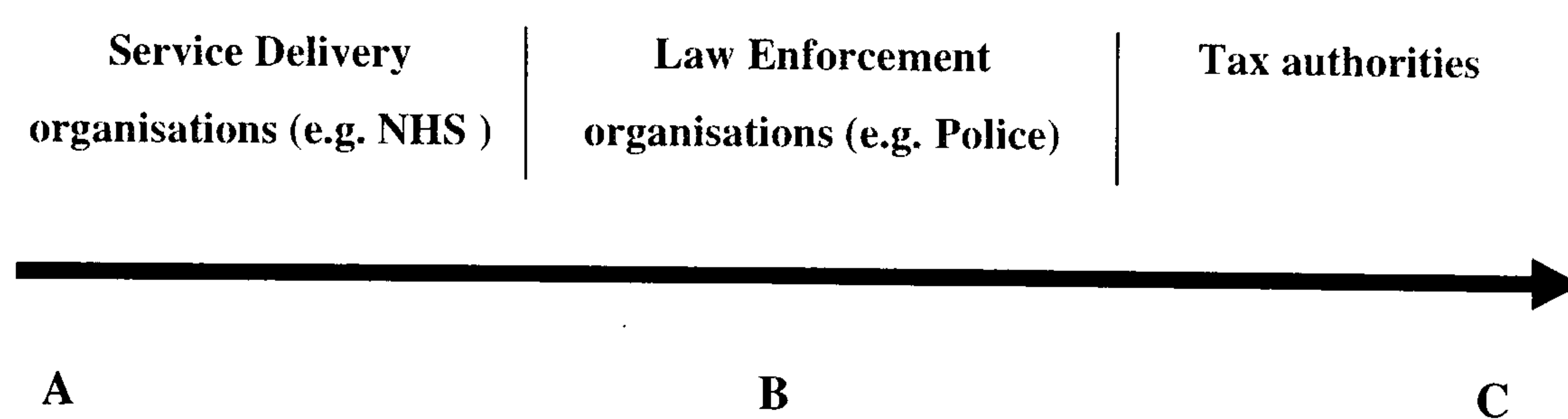


Fig 8.1: Reciprocal-accountabilities based classification of public sector organisations

On the increasing intensity line, point A represents the weakest form of such a relationship and point C is the strongest form. The *service delivery organisations* like NHS, Schools, etc are accountable to the recipients for provision of high quality services, but the recipients do not have any formal accountability relationship to them which are operationalised by formal accounting systems. At the most they are expected not to defraud these services, in which case they can be held to account. But this is not a regular form of ‘giving and taking of accounts’. In the middle are *Law Enforcement organisations* such as the Police. Though there is some degree of reciprocity of accountability between the recipients of services and these organisations, there is an important distinction as well. The recipients here demand these services of their own accord, and do not resort to avoiding receipt of those services. For instance, more police patrols and quick response to help calls are considered valuable services by the people in general. Moreover, no regular returns are filed by residents of an area to the police. On the line, point C represents the strongest form of *reciprocal accountability* as both service providers and recipients are held to account by virtue of formal accountability arrangements. For instance, in the case of HMCE, minimising tax evasion by cash based businesses and tax avoidance by the large firms are the main policy goals of compliance strategy (HMCE, 2002e: p 13).



The taxpayers are held to account by returns filing and risk based audits. On the other hand the tax authorities are also held to account to the taxpayers by formal accounting methods (*customer- focus based accounting*) such as PSA policy targets like taxpayers' satisfaction and *compliance costs* reduction, number of complaints and service charters which are scrutinised in parliamentary committees' hearings.

The literature on public sector accountability, reviewed in Chapter 2, is primarily focused on organisations situated on point A to point B. The underlying assumption there is that the organisations are accountable to the recipients of services/goods. However, if the analysis is extended to the public sector organisations on point C, the traditional analytical tools are not sufficient because in such organisations accountability is reciprocal. Drawing upon the previous discussion, the accountability system of a tax administration like HMCE has been summarised in the fig 8.2. The system can be seen as comprising of three main forms of accountability relationships, *managerial*, *legal* and *public* among taxpayers (the clients of HMCE for tax payment purposes), the tax officials, the Board and the Government.

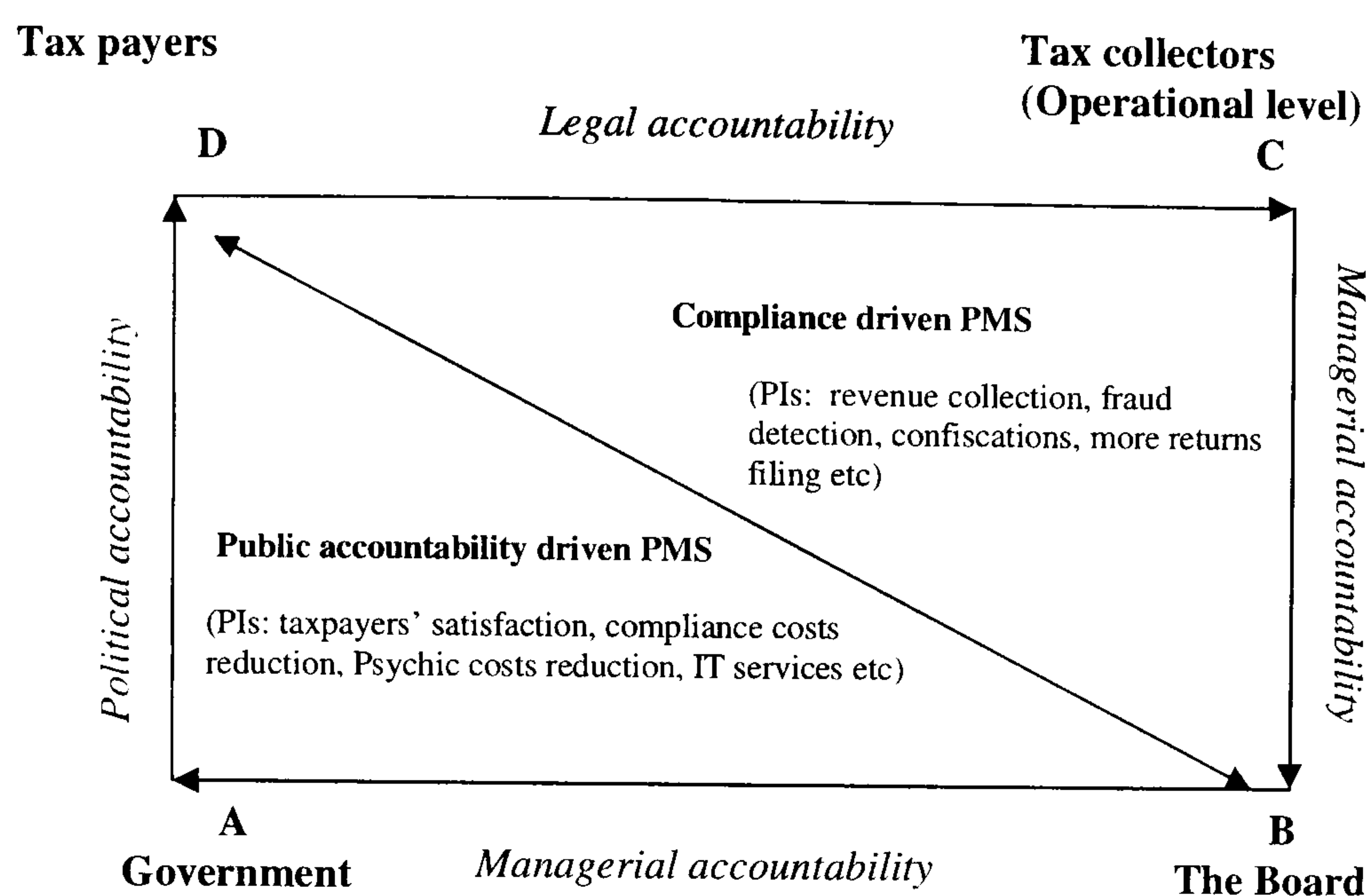


Fig 8.2: *Reciprocal Accountability Framework* developed by the PhD author

Two forms of accountability relationships are of special interest in the framework with regards to a tax administration. First is the ‘legal accountability’ relationship which is the traditional form of accountability (derived from legal powers). In this form the taxpayers are held to account through compliance enforcement by the department. The second is the NPM inspired customer-focused accountability<sup>76</sup>. The striking feature of this framework is that the taxpayers and the department are in the state of *reciprocal accountability* to each other. In the legal/traditional form, the taxpayers, like an agent, have to give accounts to the department, who act as a principal. In the political (or public) accountability relationship, the roles are reversed, and now the department acts like an agent and has to give accounts to the taxpayers, the principal, which are scrutinised by the parliamentary committees on behalf of the taxpayers.

<sup>76</sup> The managerial form of accountability essentially is an intermediary form which is an extension of either traditional or customer-focused accountabilities.



The Board has a peculiar and important position in this framework. Seen as an extended arm of the government it is actively engaged in tax policy making. Moreover, it oversees the operational activities of the tax auditors (called VAT assurance officers) and can influence their activities through managerial accountability. It can therefore be argued, that the Board is accountable to the taxpayers for the tax policy of the government and activities of the tax collectors. Consequently, the Board and Government, together are held to account by the tax payers (through parliamentary committees)<sup>77</sup>. The lower half of the rectangle represents this form of accountability relationship between the tax policy makers and the tax payers.

On the other hand, the taxpayers are also accountable to the Board. The powers of holding the taxpayers to account for their tax liability are entrusted through Acts of the parliament upon the Commissioners of HMCE who are members of the Board. The taxpayers are made accountable with the help of operational level personnel of HMCE. It can therefore be concluded that the Board and Taxpayers are accountable to each other reciprocally. The two-directional diagonal BD represents this reciprocity between the Board and the taxpayers.

The managers of all public sector organisations have to respond to cross pressures of multiple accountability relationships (Romzek and Dubnick, 2001). In the context of HMCE, the RAF rectangle can be seen as made up of two triangles which provide the orientation of the PMSs used to operationalise the relevant accountability relationship. The triangles reflect what is *central* to the relevant definition of performance and identification of what will be measured?

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<sup>77</sup> This is not just a theoretical proposition, as the parliamentary hearings are attended by both the Economic Secretary (minister of HMCE) and Chairperson of HMCE.

The upper triangle represents the traditional form of accountability relationships and all policies associated with this aspect of performance. Since this PhD concerns use of accounting information to operationalise accountability, only PMS is taken into account here. The PMS influenced by traditional/legal form of accountability will have performance measures/PIs which account for compliance of taxpayers to the tax laws. Examples are, revenue collection figures, anti-evasion cases, audits conducted etc.

The lower triangle represents NPM inspired and relatively newer pressures of accountability upon the tax managers. Here the tax payers can be thought of as members of the citizenry, enjoying legal rights which can be classified into two categories. First, civil liberty rights, which are guaranteed by laws other than revenue laws, such as Human Rights Act, 1998 and common law. By virtue of these rights the taxpayers, as free citizens, enjoy certain rights of privacy of person and property which can not be violated by any authority, including tax authorities (OECD, 1990). Second, strict tax liability rights, which are best explained by Adam Smith's following observation:

“ ... Every tax ought to be so contrived as both to take out and to keep out of the pockets of the people as little as possible, over and above what it brings into the public treasury of the state”. (*Wealth of Nations Book V, Chapter 2, part II*)

Put briefly, it can be argued that while every good citizen is expected to pay the due tax in full, he also enjoys the right that in discharging his tax liability he is not forced to incur any extra monetary costs over and above the tax amount; he also enjoys the right that he is not forced to experience any psychological worries in meeting his tax liability.



Adam Smith also mentions the issue of psychic costs of taxation:

“... though vexation is not, strictly speaking, expense, it is certainly equivalent to the expense at which every man would be willing to redeem himself from it.” (ibid)

VAT is generally considered to be a complex tax system, and historically tax evasion and avoidance have been high, as is evident from the following observation made by the Economic Secretary in the foreword of a high level strategy paper of HMCE:

“We are launching a strategy to tackle the *revenue shortfalls* which – over the last decade or more – have become a *standing feature of the VAT system*” (emphasis added: HMCE, 2002e: foreword).

A senior manager made even more frank admission with respect to unpopularity of taxes, especially VAT, among general businesses:

“I would say that most people don’t want to pay taxes. Certainly most VAT registered businesses would rather not be unpaid tax collectors, so they have problems” (SM2: p 22)

The above discussion should enable us to answer the question as to what do the taxpayers, as the stakeholders in this system, want from the tax policy makers and managers. They want the tax system to be simple to understand, with a very high level of respect for their civil rights and which refrains from subjecting them to high compliance costs.

The diagrammatic representation of pressures of accountability should not lead us to believe that the tax authorities will be under equal pressures from government and taxpayers. In fact, the stakeholders do not have equal powers in influencing the decisions of managers and arguably ‘resource dependence’ becomes the dominant factor in this power asymmetry situation (Frooman, 1999). The government being the resource provider enjoys an advantage as

against other stakeholders. The taxpayers may counter this advantage of the government by utilising ‘public opinion’ pressure upon the tax department. The parliamentary subcommittees can be thought of as the most important representative and guardian of the taxpayers’ rights. For instance, the seventh report of the Treasury Committee of House of Commons is titled *The Administrative Costs of Tax Compliance* (TSC, 2004) which deals specifically with the issue of minimizing compliance costs. The importance attached to the demands of taxpayers is evident from the following lines:

“The Paymaster General told us that it was probably fair to say that reducing compliance costs had a higher priority now than five years ago and that “whilst it was always there, we are pushing ahead and trying actually to bear down on it in a more systematic way” (P 5).

The upshot of the preceding discussion is that the ‘political accountability’ of Government to its taxpaying voters is operationalised in the political process (Parliament, voting) and along channels of public opinion like the press, academic research and business associations. It can, therefore, be argued that the area of this *public accountability driven* triangle represents the policies and actions undertaken by the Government which explicitly aim to minimise the problems perceived by taxpayers to be associated with tax, like compliance costs<sup>78</sup>, excessive ‘red tape’, and corruption.<sup>79</sup> However, as stated earlier, the

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<sup>78</sup> Even the official report on merger also mentions compliance costs reduction as an important objective of merger of the two departments.

<sup>79</sup> Considering performance management in the case of Inland Revenue, Fitzgerald et al (2004) distinguish between two types of accounting in the following way:

**Customer accounting** has been developed to facilitate the customer focus imposed to reorganise IR facilities and processes, as well as to report on customer service, support and enablement. Some forms of reporting are externally mandated – e.g. customer service standard reporting. Others have had to be developed, e.g. customer support.

**Compliance accounting** focuses on another aspect of performance. Tax departments are judged on how well they collect the tax that is assessable under existing tax policy and law.



concern of this PhD is restricted to the use of PMS for operationalising accountability. Consequently only accounting information made available to the taxpayers with regards to performance of HMCE (or any tax organisation) on this dimension will be of interest in RAF.

## **8.2 The Reciprocal Accountability Paradox**

The essence of Q 4 of the six questions framework identified earlier in this chapter is to determine as to which accountability relationship is the dominant one. This can be answered by considering two probing questions:

- What measures/PIs are used by the tax department to assess its performance?, and
- How performance is reported in the narrative form?

It was identified that the diagonal BD in the framework represents the *reciprocal accountability relationship* between the taxpayers and the tax department. They are principal and agent to each other under the accountability relationships of the upper and lower triangles. Arguably, the two triangles represent potentially contrasting objectives of a tax administration, and the possible tension between the conflicting aims of a tax policy may not be easily resolvable. A recent study by CIOT (2003) is a good example of the nature of relationships between the tax collectors and taxpayers (or their consultants). The study finds that while the two groups had a sharing of views on some issues they were quite divergent on

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Some measures are externally mandated: net tax revenues raised, as well as amounts written off. An additional important element is: Has as much as possible been collected

The *Customer accounting* and *Compliance accounting* can be seen as the operationalisation of NPM inspired customer-focused PMS and the traditional compliance driven PMS of RAF.

others. The possibility of tension between notions of performance is evident from the following slightly sweetened conclusion:

“There was strong support from both tax advisers and HMCE staff for avoiding an adversarial approach and for increasing the amount of consultation with taxpayers and tax advisers before new measures are introduced” (CIOT, 2003: p 17).

The possibility of conflicting notions of performance is also mentioned by the TSC in its report cited earlier in this section.

“We recognise the conflict between producing a tax system that is simple to understand and operate, and the need for checks and safeguards to bear down on tax avoidance” (TC, 2004: p 5).

Therefore, it can be argued that due to this potentially conflicting situation, the policy managers will be faced with three possible scenarios with respect to the proposed framework.

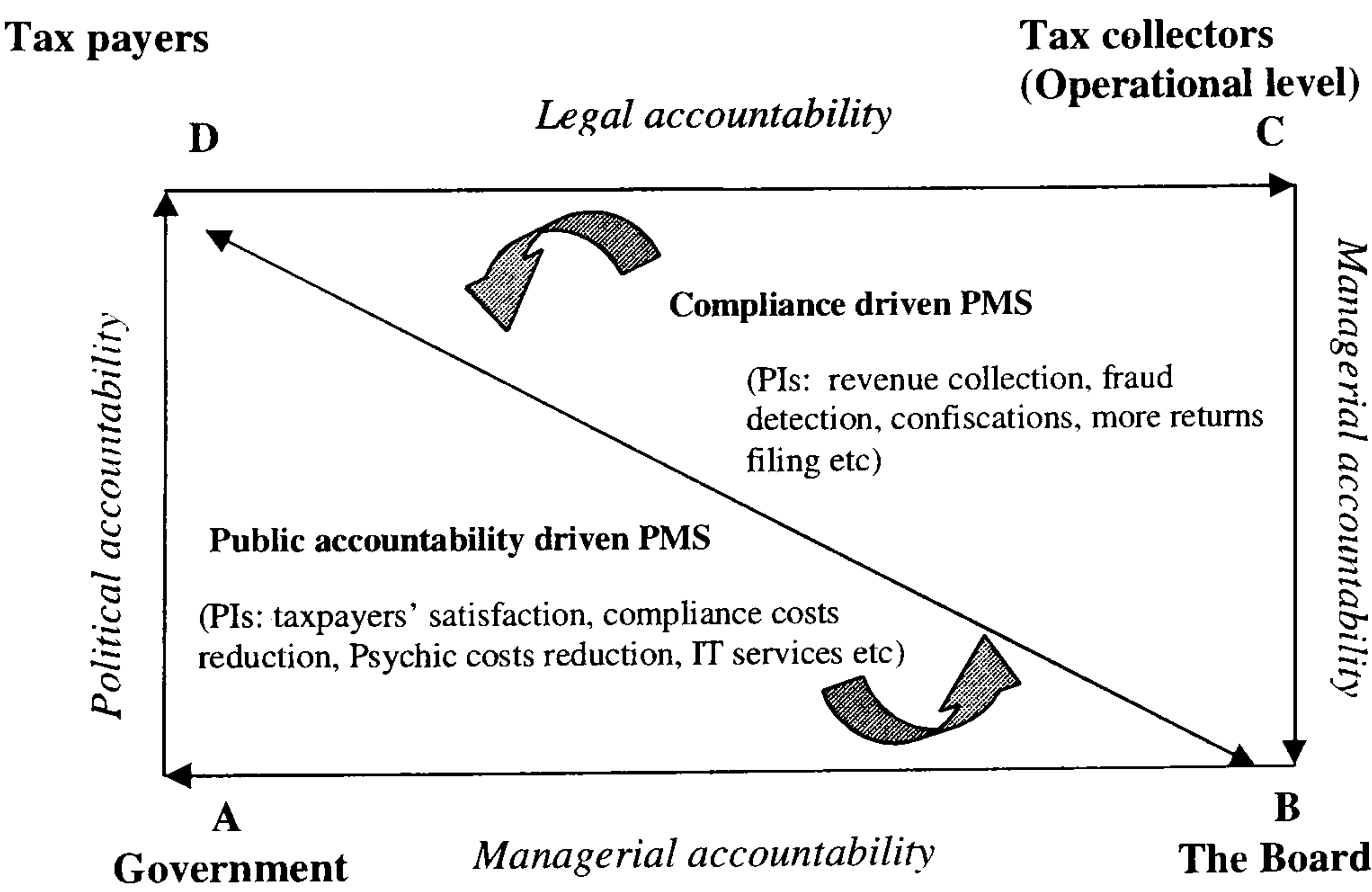


Fig 8.3: Dilemma in Reciprocal Accountability Framework



First, the desired policy of the government and the tax administration would be to ensure a trade-off between the two triangular halves in such a way that we have two symmetrical triangles. This ideal situation can be term as *Symmetrical Policy Framework*; which is achieved when concerns about compliance regulations and public accountability are equal in magnitude thus the *reciprocity diagonal* which establishes a two way mutual accountability relationship between the taxpayers and the tax policy managers (i.e. the Board) stays intact. In this situation the PMS of the tax administration will have PIs which relate to the two halves in equal importance. This means that not only there will be PIs indicating compliance and taxpayers' satisfaction but that they will be given importance in textual narratives and rewards/penalties will be linked to the two as well.

Second possible situation can be when the concerns about revenue enhancement through greater enforcement outweigh public accountability concerns. If the measures/PIs are all related to compliance enforcement (e.g. revenue collection, detections, seizures) then it is an indication that the traditional form of accountability dominates the system. This can be termed as *Compliance Dominant Policy Framework*. In its extreme situation, in the Fig 8.2 the *compliance driven* part of the rectangle will squeeze out the *public accountability* area of the rectangle. The tax policy managers feel themselves to be only accountable to the government and the tax policies and PMSs of tax authorities reflect tax revenue generation as the only policy goal.

Third possible situation can be termed *Public Accountability Dominant Policy Framework*; when the revenue enhancement concerns are less influential as against concerns about respecting civil rights of the taxpayers and wooing

investors. In its extreme hypothetical situation all the measures/PIs are related to *public accountability* concerns (e.g. taxpayers satisfaction, compliance costs reduction, complaints handling) and thus the *compliance driven* part of the rectangle is squeezed out by the *public accountability* area of the rectangle.

A fact noticeable in the framework and often found in the official discourse of the tax authorities is the desire for pursuing symmetrical policy framework where both enforcement and taxpayers' problems would appear high on the policy agenda of the tax policy managers. But the paradox faced by the policy makers is that they find it difficult to increase the area of one triangle without shrinking the size of other. It's not to suggest that a tax policy maker always intentionally wants to see asymmetry between the two triangles. The point to stress is that both compliance driven and public accountability driven policies entail unintended consequences which impact the area of corresponding triangle.

It is often seen that when tax policy makers launch a compliance/enforcement drive, there can be a resulting perception among the taxpayers that any improvement in compliance performance is achieved by the department at the expense of the taxpayers' civil legal rights or increased compliance costs. This point can be illustrated with the help of efforts made by HMCE in combating *Missing Traders Fraud* which will be discussed in the next chapter. The department prominently mentioned the success of efforts made towards minimising this large scale fraud in its annual reports. But there were some unintended consequences of the drive as can be noted from the following excerpt of a story appearing on the *AccountingWEB.com* (20-Aug-2002)



“The legitimate mobile phone industry is being affected by Customs' overreaction to the fraud. Tax consultant Don Mavin claims Customs is panicking and refusing to pay out legitimate VAT repayments until checks have been made on the entire trading chain”.

Another story appearing on the *AccountingWEB.com* (22-Apr-2003) illustrates the point more clearly. The story claims in its opening paragraph that:

“Customs & Excise is being given draconian new powers to combat VAT fraud. Measures in the Finance Bill published last week threaten to hit legitimate traders – especially in the fraud-riddled computer chip and mobile phone industries – for VAT losses caused by the activities of criminals, reports *The Independent*. These measures will allow Customs to impose liability for payment of lost VAT on suppliers or recipients of goods either side of a missing trader, even if they were not knowingly involved in the fraud”.

The high level strategy papers<sup>80</sup> of HMCE state that anti-avoidance strategy is one of the pillars of the new VAT strategy (HMCE, 2002: p 16). While pursuing this strategy the intended goal is to achieve improved performance on compliance side of the accountability framework. However, as an unintended consequence there can be apprehensive perceptions among the taxpayers or their representatives as well. This is suggested by the following remark of Hugh Love, a tax director at PricewaterhouseCoopers and a former senior Customs officer in the aforementioned story.

“Customs have been over-enthusiastic in their anti-avoidance operations lately. What I fear is, if they do not like a trader's response or it's a bit slow, they will use these new powers too broadly”.

Similarly, in a written evidence before TSC, PricewaterhouseCoopers remarked that HMCE “*has a culture of seeking to maximise the tax collected rather than collecting the tax that is properly due under the law*” (TSC, 1999c).

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<sup>80</sup> These high level strategy papers will be discussed in the next chapter.

The PhD researcher, with the help of the secretary of the VAT practitioners group, obtained written answers from 20 tax advisors (annex 10.2). The generally shared theme of the replies was that the HMCE's performance was driven by the Treasury demands for more tax revenue while the taxpayers' legal rights were by and large ignored

In view of the above evidences it can be argued that the tax authorities are faced with the paradox of maintaining a symmetrical framework in a situation where good performance on one triangle of the framework might be perceived as infringing upon the area of the other triangle.

### **8.3 Conclusion**

In this chapter a framework for analysing accountability relationships was developed with the help of insights from structuration theory, stakeholder theory and principal agent model. The skeletal framework is fleshed by empirical evidence of accounting changes implemented by HMCE during the period of analysis of this PhD research. If the PIs of HMCE discussed in chapters 5 and 7 are re-examined, it can be seen that the *Next Steps* and CSR (1998) PSA were compliance driven as compliance enforcement related measures were not only prominent in measuring performance but the textual reporting in Annual Reports was also done with reference to these measures alone. However with SR (2000) PSA it can be said that a conscious effort was made by the reformers to shift the focus of performance measurement from traditional form of accountability to the customer-focused one. The measures/PIs listed in SR (2000) PSA do suggest such a shift. However, it is important to notice that the narrative reporting in the annual reports continued to be dominated by the traditional measures of



performance. The tensions created by the new PIs were discussed in the previous chapter. To what degree the shift in focus permeated the ethos of the organisation needs analysis of further evidence which will be dealt with in the next chapter. This further analysis of evidence is required so that it is known how did the department cope with the accounting changes of SR (2000) PSA (Laughlin, 1995; Oliver, 1991).

## Chapter 9

### **Reconciling the Tensions – the Tax Gap Based PMS**

#### **Introduction**

In the previous chapters it was argued that the performance measurement of HMCE moved away from outputs to outcomes based multidimensional framework. The shift in focus from traditional form of accountability to the NPM inspired customer-focused PSA resulted in tensions between the two forms of accountabilities. It was also learnt that the accountability relationships between HMCE and its clients *the taxpayers* characterised an element of *reciprocity*. Traditionally, the focus had been on the compliance enforcement side of this reciprocal relationship. How did HMCE cope with this shifting of focus towards customer-focused PMS is the focus of this chapter. Three types of evidence are examined for this investigation purpose. First, the views of the employees are analysed to identify if the accounting changes had any visible effect on how performance is conceptualised by them. Second, the accounting changes themselves are analysed to see what happened to them and how they were used or redefined. Third, the merger of HMCE with Inland Revenue is briefly investigated to see if it lends substance to the conclusions. The overall evidence helps in concluding that the PMS introduced by PSA 2000 failed to make any significant impact upon the traditional ethos of HMCE.



## **9.1 The Notion of Performance**

Acknowledging the fact that ‘performance’ is capable of no simple definition, Otley (1999) suggests that an organisation that is performing well is one that is successfully attaining its objectives. The notion of performance articulated in the official publications is influenced to a great extent by the private sector models of performance management (Likierman, 1994; Bromwich and Lapsley, 1997). It was stated in chapter 6 that in the latest official performance reports of HMCE, organisational performance has been construed in terms of implementing organisational strategy as spelt out by PSA aim and objectives. For instance, the Spring Report, 2003 outlines the new strategy based conceptualization of performance:

“We have adopted a strategic approach to our responsibilities and reformulated our main targets to be outcome based. This means we assess and quantify the size and nature of the problem to be tackled and determine an appropriate strategic response that drives outputs and operational interventions to deliver quantified outcomes. Output based targets are used as management indicators – it is the outcomes that are the goals ...The Government has invested in our approach. This is reflected in our new Public Service Agreement. It focuses first on compliance, second, on improved efficiency and third, on service quality” (HMCE, 2003b: p7).

The Annual Report refers to this new conceptualization of performance by comparing it with the traditional meaning of performance.

“Traditionally we measured our performance in terms of the level of certain activities: smuggled goods seized, numbers prosecuted and efficiency gains achieved. In 2000 the Department changed fundamentally its approach to setting objectives and measuring performance” (HMCE, 2003c: P7)

The shift in meaning of performance is also orchestrated in the discourse of very senior managers. For instance one such respondent referred to this process of conceptualising as:

“... that it’s down to us here to, as it were, to translate the information, the information on performance measurement, we get from regions, to translate that into national picture, so that we can say, that we are on track to meet our national departmental objectives, or not, ...” (SM1; p 1).

The description of the notion of performance from the top level official discourse would suggest that the new notion of organisational performance is conceived with clarity across the whole organisation. But when the same question was put before the middle and operational level employees the notion of performance was defined by the respondents in their own particular ways which arguably reflected their nature of jobs, personality types and experience. Some defined performance in terms of *more returns and thus more revenue* (MM7), others equated it with *number of audit visits made* (MM1), still others viewed it as *meeting the quantitative target allocated to the office* (MM3), some defined it in terms of meeting objectives but had difficulty in detailing objectives (OL1). Still others found defining performance very difficult (OL5).

The importance of ‘bringing in money’, the traditional form of accountability, is still a recurrent theme in the discourse of operational level employees:

“I think most of the time even in the past we have always been judged on the number of hits, basically have you received an assessment or not and I think it still goes on even now they are saying well the money doesn’t really matter, although they still want the money they want the compliance, they want” (OL6: p8).

Same concern for ‘more revenue’ is clear from the replies of two other interviewees as well.



“Yeah, if you say, yeah I went out, I didn’t get the money but I didn’t get any complaints I don’t think you’re going to get the benefit from that really” (OL3: p22).

“I am more interested in the money ; I mean it’s not finding anything which is not there; but you are interested in finding money; because that effectively is why we have gone out there” (OL1: p13).

An operational level employee was also candid in admitting his ignorance about the PSA objectives:

“There are documents that have come around routinely... yes; there was something sent around quite recently by an email; I think I glanced through it but ...[laughingly] yes; I don’t have time to read all that sort of stuff; I know there is perceived problem with VAT gap at the moment” (OL1: p12-13).

Good performance is also construed on contingency approach basis which is quite often the case in most of the organisations. One Officer put it like this:

“I think it tends to be where you find major problems and concerns because those are the things that take more resolving, they are more immediate because you find the area, you take the action to correct it or whatever so that is what is occurring now” (OL6: p8).

In chapter 2, reference was made to Brumbach (1988) who defined performance along the dimensions of results and behaviour. The author argued that good results can be achieved through either bad behaviour or good behaviour. A success is positive when good results are achieved through good behaviour. In the case of HMCE positive success would mean achieving good results with good behaviour towards the taxpayers so that the relationship builds upon mutual trust (Daunton, 2001). Thus it can be argued that the new PSA framework desired to shift the overriding emphasis upon revenue figures to good behaviour towards the taxpayers, i.e. from mere *results* to *positive success*. The review of the notion of performance held by the operational level employees suggests little that this transformation was actually achieved.

It was argued in the previous chapters that the main aim of PSA framework was to implement the customer focus ideal of NPM styled reforms. However when the interviewees were asked to express their views on the notion of ‘customer focus’, there was a general lack of enthusiasm for the phrase. Historically, as was noted in chapter 4, ‘customer’ was one of the key customs officers in the medieval days. Under NPM, all recipients of services from public sector organisations are considered as customers (McGuire, 2002). Some HMCE managers, while remaining sceptical over complete relevance of such terms, did try to defend the usage of the phrase. For instance, one manager replied with an expressly official tone:

“.... yes; I mean this is where, as I spoke to you earlier on, where the move is I suppose move away from us putting so many of our people out to the businesses to conduct audits with the prime objective of hopefully finding additional tax; to actually moving a lot of those into areas of compliance management which is very much customer-focused activity; it is activity whereby we want a different approach from our offices; we want them to be very nice and very friendly with the businesses and improve our image in that way”(MM1: p 12 ).

Another manager while accepted that lack of choice for taxpayers as problematic, yet he defended customer-focus as a useful concept:

“...I see your point, that you don’t have a choice. Okay, you don’t have a choice but that shouldn’t taint my view as to how I treat you. I shouldn’t treat you with the sort of contempt that well, you’ve got no choice and you will do this; won’t you? Don’t give me any of your problems please, just do this for me. That’s where I think the customer emphasis comes in..... So I can see where traditionally it does not fit the terminology of customer, because you don’t really have a choice, but I think it’s the right terminology to use because that puts us in the frame of mind of dealing with people in the right manner” (MM6: p 25)

But many managers were sceptical about the phrase, as is clear from the following reply:

“Any people that we deal with are in theory our customers and it’s not a word I can use... They’re not customers. They’re the traders, they’re the people that we visit... I wouldn’t call them a customer. I know it’s a buzz word now... But I’m not in favour of it... You know we’re intruding on them and I wouldn’t say that they wanted us” (MM7: p 33).



A middle manager when asked to comment upon customer focus as an organisational ideal was frank in sharing his disdain for the new private sector jargon:

“... it all started with, when we as a department decided to accept the American business schools influence;... that for the last number of years the department has been using outside business practices and outside business techniques and outside business jargon in order to try and introduce some professionalism into the department; it has failed to increase the professionalism or it's like the silly jargon words that do not apply” (MM4: p 21).

When an operational level employee was asked about his notion of customer focus he spontaneously replied “*That doesn't mean anything to me*”. When the phrase was explained to him he replied:

“... customer focus to me is a marketing tool; (a pause) not a marketing tool but a way of looking at customers; (after deep thinking) I don't think traders are customers to Customs and Excise in a way; they are registered businesses and they have to pay VAT; I don't see them as customers; they are operating businesses; it's a government regulation that they have to be registered and therefore they will pay VAT and as a part of that they can have inspection obviously to find out if their returns are right ; as I said customer focus to me is a marketing term” (OL2: p 10).

Another important notion interrelated to the notion of performance is that of *accountability*. This research found that the employees of HMCE viewed accountability mostly in its managerial sense and appreciation of other forms of accountability were less pronounced. For instance one manager replied that:

“I think it [accountability] is two way. I am directly accountable to, and the person, I am first accountable to, has got to be my manager ... but I also feel that I am accountable to my management team here; the other managers across this division, I am accountable to them ...and we do operate as a team we also meet in a formal meeting at least once a month and we will take decisions about how we are going to do things within this division; within the parameters that we are allowed to work within, so it's a bit of a mix of both; I am accountable to those that are with me locally and also to my manager” (MM1: p 16).

The interviewee defines accountability in terms of managerial responsibility to the superiors and sub-ordinates. Same emphasis on managerial meaning of the term is evident in the following reply of another manager:

“I think the general sort of well-being and management of the team is where the accountability stands” (MM3: p 39).

Some interviewees understood accountability in terms of performance appraisals (PA), as the following reply suggests:

“well ! [accountability is] to my line manager; I mean she is the one who is doing the PA [performance appraisal] meeting on Tuesday” (OL2: p 17).

The issue of controllability also surfaces in the reply of one interviewee. Raising lack of effective control on events as a major concern, the manager airs anxiety over the multiplicity of accountability expectations:

“... I mean I have to accept that I am accountable for things that happen around me that I'm not readily in control of, like Health and Safety issues. If anything happens to any of my people then it's down to me ultimately if there's been a problem, then I've got to be accountable for it. I have to be, I have to provide assurance that the budgets allocated and what we spend on travelling and subsistence are correctly spent within the parameters of the instructions. I'm accountable for the actions of my people on the ground. So if they get lots of complaints, well yes, they'll be under the microscope but so will I. What have I been doing about it? I'm accountable for their development. I'm accountable for their input to our business and the Plan, and so I think you're accountable on a huge field of issues and basically the buck stops with you, ... I'm accountable for their [subordinates] behaviour, if I'm with them and I witness bad behaviour then I'm accountable for addressing it...Well I think the pressure is that I feel like I'm accountable for everything” (MM6: p 26).

Some managers viewed accountability as meeting quantitative targets. For example one manager remarked:

“My accountability and what I strive to do is to achieve the targets, That's what I'm there for” (MM7: p 38).



A few respondents did try to view accountability in a wider perspective but the emphasis remained on managerial accountability, as is evident from the following lines:

“... Really [accountability] goes in various stages. So here, I mean we’re accountable directly to our manager but then there’s a whole wider picture above that in terms that there’s a higher management but then there’s the Government and the Ministers and then ultimately there’s the taxpayer out there as well... Yeah I mean the only one that really impacts greatly on you is your own manager because you get the feedback and things from that” (OL3: p 25).

It was documented in chapter 4 that the department performs diverse functions and has different work pattern regimes. A manager stated that the common belief of protecting society from the nefarious activities of fraudsters and criminals held together various strings of functions and sub cultures within the department

“... but at the same time there’s a common theme, isn’t there, which is I suppose the protection of society and ensuring that the right tax is paid at the right time. There’s this common thing that holds it all together, and I think the other area that’s coming through as well is that they’re all business tax-related and we’re purely looking at the taxation, whether it be Excise reliefs, or whether it be Customs duties or, when you start bringing in the prohibitions and restrictions it broadens it out a little bit more, but in essence these are the consistencies within the department across the board” (MM3: p7).

Thus it can be seen from the analysis of the discourse of the operational level employees of HMCE that the PSA based accounting changes did not change the notions of *performance* and *accountability* relationships as the employees continued to define the notions in terms of the traditional ethos of law enforcement.

## **9.2 From Customer-Focus to Risk Management**

In the earlier chapters it was found that the SR 2000 introduced ‘outcomes’ based PMS in the form of PSA 2000. The new PMS gave prominence to customer-

focus based PIs and relegated the traditional revenue collection figures to a Trust Statement. It was also found that the new PIs put HMCE in a difficult situation. How did the organisation cope with the tensions created by PSA 2000 is the aim of this section.

In 2001 HMCE published a high level policy document titled *Tackling Indirect Tax Fraud*, (TITF) (HMCE, 2001d). This was the first document which described the Government's strategic approach to tackling revenue losses, which was based on:

- accurately assessing the size and nature of each problem,
- setting clear objectives and targets for tackling it,
- identifying the operational responses required to achieve those targets and
- monitoring the delivery of results.

The policy document was followed by *Protecting indirect tax revenues*, (PITR) in November 2002 (HMCE, 2002e) which extends the strategic risk management approach applied in the case of cigarettes/Tobacco smuggling and Oil Smuggling to all indirect taxes, most importantly VAT.<sup>81</sup> A new VAT strategy (Annex 9.1) is announced which lists the main sources of revenue losses as:

- VAT missing trader fraud<sup>82</sup>
- VAT avoidance

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<sup>81</sup> The publication has three sections. In Section 1 the importance of strategic approach to revenue losses is explained. In Section 2, *Excise* duty losses with respect to Tobacco, Oils, and Alcohol smuggling are discussed and the strategy to minimise the losses is laid down. Section 3 builds upon the claimed success of strategic focus in the case of Tobacco and Oils and is extended to VAT losses.

<sup>82</sup> *Missing Trader Fraud* is mentioned as an EU-wide problem, in which bogus traders register for VAT, complete intra-Community transactions, and disappear before paying over the VAT due to the tax authorities. An interviewee commented: "It's a major, major VAT problem... I did gold frauds which were big in their day, but these are even bigger" (MM5: p8). The details of this type of fraud and other VAT losses can be read in Annex 8.1.



- Other VAT losses

These policy documents prescribe risk management as the basis of strategic approach for HMCE. The new PMS introduced by PSA 2002 and the subsequent annual reports of HMCE are based upon this risk management approach (HM Treasury, 2002a). In fact, the Annual Report, 2003 describes HMCE as a risk management organisation whose aim is declared as achieving the status of ‘the best risk manager in the public sector’, comparable to the best in the private sector (HC52, 2003: p 7). In the *Resource Accounts* reported in the Annual Report, 2004 it is claimed that the department has sought to raise its standard of risk management to equal the best in the private sector (HC119, 2004: p 47)<sup>83</sup>.

An OECD publication defines the phrase ‘risk management’ as:

“...a formal process whereby risk factors for a particular context are systematically *identified, analysed, assessed, ranked* and *provided for*... It is a proactive, systematic analysis of possible events and responses to them rather than a mere reaction mechanism to those limited events that are detected” (OECD, 2001: p 3).

With the latest version of PSA in 2002, the shift from customer-focus to risk management is complete. Risk management requires not only identification of risk areas but also the ability to measure success in minimising those risks. Therefore, just as the PSA objectives and policy targets have been defined by reference to high level strategy papers, the new *Technical Notes* document which accompanies the PSA (SR2002) refers to publications *Measuring Indirect Tax Fraud* (HMCE, 2001e), and *Measuring Indirect Tax Losses* (HMCE, 2002f).

These documents explain how performance against specific targets would be

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<sup>83</sup> The increasing emphasis upon strategic risk management is evident from the HMCE’s latest Annual Reports, as well. The term *risk* has been used 271 times while the phrase *risk management* has appeared 37 times in the latest 2004 Annual Report, while the two terms were used 260 and 28 times respectively in the Annual Report 2003

measured. The policy targets under the three objectives of PSA specify the targeted level of performance required for achieving the stated objectives.

HMCE claims that the new PSA has even sharper focus on strategic aim of the organisation (HMCE, 2003: p 7). But before the significance of the new PSA is analysed it seems necessary to first examine the measures and PIs used in this version of PSA so that its difference from the earlier versions of PSA becomes clearer.

The policy targets under the three objectives of SR 2002 PSA specify the targeted level of performance required for achieving the stated objectives. The levels of performance desired under the new PSA have been tabulated by the researcher and produced in table 9.1.

Objective		Policy Target	Targeted Item/service	Desired level of performance	Targeted Date
No	Title				
1	compliance				
		Reducing illicit market as proportion of total market	<i>oils</i>	2%	31 March 2006
			<i>tobacco</i>	17%	31 March 2006
		reducing the scale of VAT losses		12% or less of the theoretical VAT liability	from March 2003
		Improve Customer service	<i>Electronic service delivery through a common Government portal</i>	100%	by 2005
			<i>take-up for key electronic services</i>	50%	by 2005
			<i>Reducing compliance costs</i>		
2	Anti-drugs trafficking				
		Reduce the availability of illegal drugs	<i>Increasing the U.K bound heroin and cocaine seizures</i>		



			<i>disruption/dismantling of criminal groups involved</i>		
			<i>the recovery of drug-related criminal assets</i>		
<b>3</b>	<b>Value for Money</b>				
		productivity gains without affecting customer satisfaction		2.5% a year	

Table 9.1: Targeted levels of performance under PSA 2002 (adapted from HMCE, 2002g,h)

As is clear from the table, the **first objective** (*compliance improvement*) is to be achieved by setting up two subsidiary strategic policy targets. The first one aims at minimizing tax losses in the case of Oils, Cigarettes and VAT. Time bound quantitative targets for the three have been provided under this policy target. The first two aim at reducing the market share of illicit oil and cigarettes to 2% for oils and 17% for tobacco; while the third deals with VAT losses reduction. *Measuring Indirect Tax Losses* (HMCE, 2002f) explains how the *tax gap* has been measured. The causes of the VAT losses are categorized as due to error, ignorance and financial difficulty or due to wilful default like abusive avoidance and deliberate fraud. The tax gap can be, therefore, minimized by minimizing the scope of both types of tax losses. The specific target is to reduce the scale of VAT losses from the 2002 baseline of 15% to 12% or less of the theoretical VAT liability which in turn amounts to collecting more than £2 billion per year in additional revenue by 2005-06.

Target 2 under the first objective of *compliance improvement* is based upon service delivery improvement. Therefore, the implied assumption is that

compliance with indirect tax liability will improve if the taxpayers are provided with better services. The influence of NPM inspired private sector performance frameworks is quite evident. The customer service has two ingredients listed as measures. First is the provision of services through electronic delivery<sup>84</sup> and second is minimising the costs of complying with indirect tax regulations. For the first measure the targets are specific, i.e., 100% provision of electronic services by 2005 as against baseline 61%, and at the same time achieving take up rate of 50% by 2006. The second measure of compliance costs reduction is however without any target and seems more like a wishful declaration.

The only target under objective II refers to reducing availability of illicit drugs. The three performance indicators for this measure are *seizing drugs being supplied to the UK market, busting criminal gangs involved* and seizing assets made out of drugs related money.

Target 4, which is the final target comes under the third objective of *Value for Money* category and aims at achieving productivity gains of 2.5% per year. In view of the embarrassing results reported in the earlier PSA, this time the initial technical note did not provide details on how this would be worked out, and instead promised that the same would be made available in a revised technical note in the near future (HMCE, 2002g,h). Finally when the *Technical Notes* document was updated it explained that Progress against the target will be assessed mainly in terms of staff year savings and procurement gains. It is

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<sup>84</sup> The emphasis on IT reforms is also clear from the title of a recent NAO report “*Transforming the performance of HMCE through electronic service delivery*” As a final conclusion, the NAO study is appreciative of the reforms however it adds a cautionary note that: “Our ‘health check’ of the e-programme showed that development of the business case and benefits realisation plans are the main areas which the Department need to address” (NAO, 2003: p 10).



mentioned that delivery against the target would be monitored through the monthly management accounts and a programme of quantitative and qualitative customer surveys would be used to monitor *Customer satisfaction*.

### **9.3 Tax Gap – an Assessment**

The new PSA of HMCE is claimed to be based on the strategic risk management approach of ‘Tax Gap’ reduction.<sup>85</sup> The effect of the change is that the PSA of the department got drastically changed as the organisational performance was redefined in terms of closing the *Tax Gap*. Arguably, the new language employed appears to be quite appealing and explanation of this new approach in strategic management terms is quite persuasive.

The tax gap was defined in chapter 6. In this approach, a *theoretical tax yield* is first worked out under the assumption of 100% compliance with no intentional avoidance or evasion, or unintentional errors based losses of tax revenue. This is then set against the actual outturns. The difference between the actual and theoretical tax yield is termed *tax gap*, and the single strategic policy aim is to plug the gap with the help of what the tax policy managers call *compliance management*. The high level strategy papers of HMCE (TITF, PITR and VAT Strategy) contain detailed accounts of VAT gap. According to the VAT strategy document:

“The amount of VAT that is lost through organised fraud, avoidance, general non-compliance and failure to register has been estimated by comparing the theoretical tax yield, calculated using ONS National Accounts data on total expenditure in the economy, with

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<sup>85</sup> The ‘Tax Gap’ approach is not a ground breaking approach as many other tax authorities (e.g. Swedish Tax Administration) were already following it as the basis of their performance measurement (OECD, 2001: p 36).

actual VAT receipts. For the year ending March 2001 the size of the 'VAT Gap' is estimated to be £10.4bn, 14.6% of the theoretical tax yield. Historically, the VAT Gap rose sharply from 10% to 14% in the early 1990s and has fluctuated between 12% and 14.5% over the last 6 years (VS: p1)

The strategy papers talk about considerable new resources to institute a concerted strategy to tackle the problem of tax gap. The new risk management approach is therefore driven by a concern for minimising revenue losses, which in effect means increasing revenue collection figures. Strong law enforcement measures form an important part of the new strategy together with enabling approach (Hoskin et al., 2001) to help those who are potentially compliant taxpayers.

Pollit (2002) groups together various theories such as institutional economics (e.g. Principal agent and property rights theories), contingency theory, and rational choice theory as a functional theory of organisational change. . The common feature of this category of theories is that they all explain a phenomenon in terms of intended results.

According to these theories the search for new practices is governed by rational choice making. The institutional theory, discussed in chapter 2, is a competing theoretical lens which has gained popularity among writers of various disciplines such as economics, political science, marketing, organisation theory and sociology (Scott, 1995). The essence of this theory is encapsulated by Scott (1987) who contends that organisations change : "...because they are rewarded for doing so through increased legitimacy, resources, and survival capabilities" (p. 498).

In chapter 8, two potentially competing PMS were identified in the RAF. But when a tax management system is viewed from a functionalist perspective, the



tax payers and the tax collectors are believed not to be in any state of competition or conflict of interests. The underlying belief can be best explained by making a reference to the social exchange theory<sup>86</sup>, discussed in chapter 2. The government gives the tax administration economic resources to collect tax revenue with which it finances its public programmes. The citizens in the capacity of taxpayers can be seen as not ‘paying customers’ but rather as ‘obligatees’ who provide ‘compliance’ in return for good services and fairness from the tax authorities. The tax authorities can obtain compliance through coercive means like more audits, arrests and imposition of penalties. However all these methods are costly and are to be used as a last resort against wilful evaders. ‘Voluntary compliance’ not only improves efficiency of the tax administration but it also results in exchange of other values as well. For instance, other taxpayers feel more confident about the tax laws enforcement while the citizenry at large benefits from wealth distribution effects. Thus the notion of customer-focus oils the wheel of accountability in the proposed accountability framework. The citizens as taxpayers exchange voluntary compliance with the tax authorities in return for equity, good behaviour and services. This helps the tax authorities in providing good results to the Government on the traditional/financial performance dimension in two ways. First, the tax revenue itself increases. Second, voluntary compliance decreases the costs of collection, thus resulting in savings and improving productivity. The government can then also provide good results to the citizens in terms of public spending, on one hand, and the citizens in return also demonstrate less political hostility to taxation.

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<sup>86</sup> The theory emphasises a broadened notion of *social exchange* in as against the restrictive notion of *service delivery* of private sector models. A distinction between *citizenry* and *clients* is an important feature of social exchange theory. The clients are also classified into *paying customers*, *beneficiaries* and *obligatees*.

Therefore, if the social exchange theory lens is used it can be argued that the taxpayers and tax collectors are partners in achieving the common goal of financing the provision of public goods by the government. Since both the stakeholders are partners therefore the notion of 'performance' under this functionalist approach is also not a contested one. The '*tax gap*' method of measuring performance can, therefore, be seen as the appropriate measure as both the tax collectors and the taxpayers act in collaboration to reduce the tax gap.

It was noted in chapter 2 that writers using institutional theory for analysing organisational reforms underscore the importance of *context* of any particular organisation and often view *legitimacy* as the primary motive of organisational reforms (e.g. Kurunmaki et al., 2003). The difficulties with measuring and reporting performance in terms of SR (2000) PSA were discussed in chapter 8. The new customer-focused accountability for performance brought in tensions which were explained in the previous chapter. In terms of Laughlin (1995)'s framework, the sceptical view would be that the department resorted to the policy of *Re-orientation* which is a policy that aims to internalise the disturbance, through often permanent organisational changes, but in such a way that the *interpretive schemes* remain untouched and undisturbed by the alteration. It can, therefore, be argued that the new approach of tax gap approach in PSA (2002) sits comfortably with the organisational ethos of law enforcement.

While, both functionalist and NIS explanations have their respective merits, the implementation of the approach is challenging in terms of performance



measurement. For instance, an OECD publication identifies problems associated with measuring tax gap and makes the following conclusion:

“To sum up, the general position on measuring the tax gap is that it is difficult if not downright impossible and even if it were possible to get a reliable total figure it would not tell us much of practical value in the struggle against non-compliance” (OECD, 2001: p 31).

Under this approach performance is conceptualized as plugging the tax gap which in turn is measured by meeting the targets of extra revenue promised by the new strategy. Therefore overall organisational performance is interpreted through PIs that are all about extra revenue collection. Therefore, performance measurement is arguably much easier in this approach as compared to the one in PSA 2000 where customer-focused PIs resulted in embarrassing results. But ironically, when it comes to operational level PMS, the approach is keen on abandoning the ‘old’ ways of measuring success, but does not articulate in unequivocal terms what will be the alternative measures, as is evident from the following official response:

“Your references to number of visits/ assessments are no longer valid, our measures have changed to reflect the current PSA of closing the VAT Gap” (EM1).

At the official level the new strategy required new performance conceptualization and measurement, as remarked by a senior manager:

“... we said well we have got to stop this we have got to end this division here because what it means is that the strategy now becomes business as usual ; it now becomes what we are doing and everybody in this unit should be contributing in some way to the strategy and if they are not then they have got to say; why we are not doing...” (SM1; p 11)

But many respondents were frank in admitting their lack of clarity as to how performance was to be measured under the new tax gap reduction strategy, while they continued performing the same old functions:

“It’s about getting a different approach in future that will get us an outcome, and that’s difficult because we’re all conditioned to see, almost like mathematics, you can do a sum and you know what the answer is, unlike the English literature and the language, you do not know what the interpretation is, ...and we’ve been in this regimented area of mathematics and we’re coming into this bit more abstract issue, which has still got an outcome. That’s difficult for us all to understand” (SM2: p20).

The manager also cautioned against expectations of immediate results:

...and it’s going to take a long time, and it’s going to need courage from senior management, because you have, to get an outcome result, you have to wait. You have to find indicators that will tell you whether you’re on track,...(SM2: p 17).

Another manager expressed his concerns over distraction from the real job if the management became too occupied with academic debates.

“Well this year we honed it into saying, if you look at an under-declaration how much of it actually sticks with Treasury, or how much of it just goes round between traders, and what’s one person’s under-declaration is just claimed back by somebody else, so we came up with a measure called Sticking Tax. But then we’d spent most of the year trying to define really what Sticking Tax means. So we do get ourselves in a bit of a quandary over measures sometimes as to what these measures mean, and that gets a little difficult at times because we spend so much time talking about what it may be, that everybody distracts, gets distracted from the real work. So that’s the problem we have with measures, but the basic premise of what we should really be focussing on is Sticking Tax or as we term it globally the Tax gap issues, we want to close that gap of what we’re not collecting. It’s spot on. We’ve just got to do further work on refining how we measure success”(MM6: p 8).

The *sticking tax* is not the term used in the published official documents however in the discourse of managers it was found to be widely used. It refers to that amount of tax which can not only be identified by audit work but also defended in a court of law and thus represents actual increase in tax revenue. The interviewee manifestly refers to the limitations of measuring success.



A middle manager while approved of the new approach had also problems with assessing his part in the success of the strategy and thus offered his own interpretation as:

“... this strategy only started at the beginning of this year, April, that we’re hoping that we’re managing it properly and if we’re doing our job properly, then it should come down. The tax gap should reduce and the returns should be coming in and we’d be collecting more money” (MM7: p 14).

The emphasis on *more money* as an indicator of success of the strategy is quite noticeable. This is not surprising as the same emphasis on revenue figures and extra revenue collected is present in the chairman’s foreword to the Annual Report., 2003

“Net revenue receipts remained strong at some £108.7 billion (falling within the target range of plus or minus 2.5% of the forecast). This was in part due to positive economic factors, but it was largely a consequence of our compliance strategies, which are delivering impressive results..... Our comprehensive VAT strategy is now in place with the goal of securing more than £2 billion a year in additional revenue by 2005-06” (HMCE, 2003c: p 5).

A new rule/routine resulting from the VAT strategy was the contacts made with businesses that were never contacted due to costs savings driven strategy in the past. Under the old rules and routines established since the 1990s by virtue of reforms introduced by Conservative Government the majority of newly registered businesses and other small scale businesses were never contacted as they were not considered important in terms of tax liability potential. Under the new strategy they deserved attention as a matter of rule/routine and formalised arrangements were accordingly made mostly through telephones as explained in chapter 6. Since this new routine was in congruence with the organisational ethos of holding taxpayers to account, the research found its prevalence in the discourse of employees. The telephoning exercise was interpreted by the ‘holding to account’ institution of the department, as an important activity which

the department could not do in the past because they were coerced by the reforms of 90s not to do so. This is clear from the following remarks made by an interviewee:

“So there is an argument there that just by literally picking up the phone and talking to somebody there is a good chance compliance will improve because they know we are still around, we haven’t forgotten who you are and hello here we are ...”(OL5: p 7 ).

This is in stark contrast to *customer accounting* related changes introduced through PSA 2000 which failed to alter the performance data related practices and did not have an impact upon *interpretive scheme* of the organisation.

Thus it was found that in absence of clear explanation of the new measures of success the operational level employees were to a varying degree in a fix as to how their performance would be evaluated under the new strategy of VAT Gap closure, and in what ways it would be different from the old arrangements. The result was that the institutionalized notion of performance was used to interpret success as bringing in more revenue. In terms of RAF outlined in chapter 8, it can be argued that the accounting changes have made the PMS of HMCE a compliance driven framework. The new strategy’s success is measured by a single dimension of tax gap reduction, which in turn is measured and reported with the PI of extra revenue collection. As a consequence, it will not be possible to distinguish between the proportion of extra revenue which was added by enabling factors (e.g. better service delivery, greater mutual trust) and the proportion which is added by factors infringing upon public accountability driven performance e.g. measures like increased intrusiveness, or less respect for legal rights, thus lowering the taxpayers satisfaction. The notion of performance is therefore defined by the concerns of tax department while the concerns of tax



payers are not reflected strongly in the performance measures/indicators used in PSA2002.

#### **9.4 Perceptions of the Customers**

The research also collected written replies from 21 VAT practitioners. A simple questionnaire (Annex 9.2) desired to investigate the perception of HMCE among the tax practitioners. Twenty one VAT practitioners were requested to send in answers by completing the questionnaire. Due to the small size of the sample, generalizing the results for the whole population is not possible however the replies were helpful in strengthening the conclusion drawn from other sources. The premise was that the conclusions would be invalidated if the replies of the respondents suggested that the PSA related measures had penetrated the organisational ethos in a positive way so that the organisation is perceived as a customer-focused organisation and less as a pure law enforcer. However only 5 out of 21 (24%) respondents termed HMCE as a customer-focused organisation. Even these approving respondents made certain qualifying remarks. What should be worrying for the organisation is that 52% still believe it to be law enforcing organisation employing coercive methods. In another question the respondents were asked if HMCE was doing enough to become taxpayers' friendly organisation. Only 2 out of 21 respondents said clear yes to this statement while 14 respondents (67%) believed that while HMCE was trying to improve yet it needs to do a lot more before it could be termed a customer-focused organisation.

In the case of HMCE, despite adoption of outcomes based multidimensional PSA framework, little organisational effort was noticeable in the area of cultural change. The following observations were made by a respondent who had the vantage view of being an ex HMCE officer and now serving as a tax practitioner:

“I find the Department basically well intentioned towards tax payers, but hamstrung by political requirements to maximize the tax yield regardless of circumstances. As an ex-C&E officer I am also aware of a great absence in understanding of the needs and constraints of business. I have learned far more about how businesses actually operate and the pressures on them since I joined private practice, than I ever did during many years in the Department”(VP1).

The remarks are representative of the way in which the organisational culture of HMCE is generally viewed outside the organisation. These results when seen together with the in-depth interviews conducted with the employees provide evidence that the accounting changes could not transform the organisational culture which evolved from law enforcement origins.

### **9.5 The Merger of HMCE**

While this PhD dissertation writing was in progress the Government announced the merger of HMCE with Inland Revenue to create a combined department – Her Majesty’s Revenue and Custom in 2004 following a report of a review of the two departments by the permanent secretary to the Treasury Gus O’Donnell (HM Treasury, 2004). HMCE had historically been always opposed to merger of HMCE with IR. Since the parliamentary committees had been stressing the need for merger for quite some time, the interviewees were asked about the prospect of merger. They were all unanimous in their opposition to any move of merger.



For instance one manager stressed the difference in the basic nature of VAT and direct taxes:

“The VAT is a tax given to the businesses by the consumers for onward deposit with the national Kitty. Thus the businesses hold this amount of tax as a trustee, and if they don’t deposit it they commit an act of theft. The direct taxes are different as the businesses contribute a portion of their own profits to the national treasury. Hence there is a room for negotiation and lesser stringent regime of penalties” (OL6: p10).

Another manager referred to the difference in the time scale for completing audit work in the case of VAT:

“I mean they look at things so historically; generally speaking, a taxpayers record which are two years old; we look at things that are just gone; very current ; if we discover things wrong in a VAT trader’s record which are more than three years old we can’t do anything about it; because it’s out of time. The IR don’t even start looking at stuff until it is two years old and so these are some of the obstacles, some of the problems”. (MM1: p11)

Another respondent also referred to this difference:

“But I think that our time scale is a lot shorter than Inland Revenue’s. We are literally in and out ; we are supposed to be doing four visits a week and one day in the office so if I am going into a trader I have to be intrusive because I am in there, I have only got four five hours but I have got to look at everything for I am targeting specific risks; I need to assess the business as a whole but I have got to be in there fairly quickly” (OL1 : p 11).

But despite this opposition of the HMCE personnel to the idea of merger the Government went ahead with merging the two departments into one. The merger is outside the scope of this PhD study however the reasons cited in the official publication on merger are important for their evidential value. In the foreword to O’Donnell report, the chancellor cites three main reasons for the merger plan. Those are:

- Efficiency savings
- Customer focus
- Greater accountability

The efficiency argument is reiterated in the official publication which outlines the proposed structure. In the O'Donnell report a full chapter is devoted to the issue of accountability. It is stated that by separating **policy** (*for which the Treasury will be responsible*) from **implementation** (*for which the new department HMRC will be responsible*) the accountability framework will be improved. Thus the implied admission is that the accounting changes did little to improve accountability system of HMCE. Therefore the Government had to resort to the decision of merging HMCE with IR so that the culture of HMCE is improved by the culture of IR which is perceived to be customer-focused (Hoskin et al. 2001).

## **9.6 Conclusion**

The SR (2000) PSA was found to be aiming to achieve a shift of focus in accountability relationships by enhancing the importance of customer focus related measures and relegating the traditional measures of performance e.g. revenue collection figures. In terms of RAF this can be viewed as shifting the focus of accountability relationship from the traditional compliance driven part of the rectangle to the newer public accountability driven part. In this chapter three evidential sources were discussed to ascertain if the accounting changes were successful in achieving the intended aims. The discourse analysis established that while the importance of PSA related changes was evident in the official publications and senior management, no such appreciation was noticeable in the discourse of the operational level employees. By using the tax gap as the basis of performance measurement it can be seen that the department has redefined outcomes by linking it back to the traditional notion of performance. Thus the department has gone back to a single measure based



performance measurement framework abandoning the multidimensional framework of SR (2000) PSA. And finally the Government found that accounting changes could not achieve the desired aim of transforming the ethos of HMCE along customer focus and merged it with IR. Thus the three evidences together establish that the accounting changes failed to act as a force of change in the case of HMCE. In the next chapter this analysis is continued to consider the probable causes and account for the failure of accounting changes.

## **Explaining the Dilemma of Performance Measurement in HMCE**

### **Introduction**

In the previous chapters accounting changes through PSA framework were discussed and it was argued that the changes failed to transform the ethos of HMCE. This chapter discusses the reasons for failure of the accounting changes in achieving the desired aims. The discussion moves from ‘*what*’ to ‘*why*’ analysis. The second part of the chapter identifies some issues with regards to performance management. The purpose is to provide the readers with an opportunity of *naturalistic generalization* which is advocated as a merit of case study by Stake (1994).

### **10.1 Complexity and Performance Measurement**

The evidence presented in the preceding chapters established that the accounting reforms through PSA-related changes failed to shift the focus of accountability relationships from the dominant compliance-driven to the NPM-inspired customer- focused one. The notion of performance was found to be conceptualised differently by official publications and personnel at different levels of HMCE. This section examines the reasons for this lack of uniformity in conceptualizing performance and designing adequate performance measures in the case of HMCE.



Stewart and Walsh, (1994: 45) argue that performance is an elusive concept in the domain of public sector and it can never be fully defined. No wonder the policy managers in the central Government of the U.K have long been troubled by defining *performance*.<sup>87</sup> The difficulty in articulating the notion of performance in the case of HMCE is further compounded by the dilemma of achieving a balance between the compliance-driven and public-accountability driven dimensions of performance in terms of *Reciprocal Accountability Framework* proposed earlier in chapter 8. It was argued that the presence of a high degree of *reciprocity* in the accountability relationships between the *service providers* and *service recipients* ushers in further complexity to the organisation. It is not that HMCE's top management is unaware of the potentially competing accountability demands, as is clear from the following excerpt from the then chairman's foreword to the Annual Report, 2003:

"Our strategic approach to compliance now applies comprehensively to the full range of our core responsibilities: delivering agreed, measurable and published outcomes, such as reducing the market penetration of smuggled cigarettes, and reducing revenue losses as a result of fraud and other forms of non-compliance... At the same time, recognising that most businesses want to be compliant, we are working to make it easier and less costly for them to be so, not least through a major investment programme to renew and modernise our IT capacity and to provide a range of new, cost-based customer services" (HMCE, 2003c: p5).

However, articulating an all embracing notion of performance acceptable to all the stakeholders at the same time is a problem which HMCE found difficult to overcome. The existence of tension between the historically imprinted notions of performance and accountability and the new NPM inspired notion was admitted by one manager:

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<sup>87</sup> Talbot (2000) reviews the problematic nature of the notion of performance in the U.K public sector domain and concludes that there is little conceptual clarity as to what constitutes good performance. He enlists various examples, such as 3Es, customer service, BSC, indicating varying degree of emphasis on different issues at different times.

“How will we know we’re successful and we’ve started, well at Senior Management level, the Plan will be equally as much about facilitating traders as the traditional let’s find money or mistakes from them. So in theory those two parts now are equal partners, but again the problems you have is, I mentioned earlier on, that we have a very mature and experienced workforce and it’s hard to change the culture overnight, so you still feel as if you’ve done a good job if you’ve found X million of under-declared. You don’t perhaps feel as if you’ve done as good a job if you helped the trader with a problem they have” (MM6: P6).

Shifting the focus from a compliance-driven notion of performance to the public-accountability driven one is easy in theory but difficult in practice, argues the manager in his reply. But the tension is not merely between the thinking of the old guard and new strategic vision. The very nature of the work performed by VAT officers contains a dichotomous situation, as explained by one manager.

“VAT is a self assessment tax; and under the indirect control of the department, rather, as it was excise, in the direct control; we changed that, we said, o.k., well any amount of money we find is a measure of our good performance; so the conflict is that the more we encourage and succeed in getting traders to be compliant, the fewer errors there are out there to look to find with the consequence of our [ thinking of proper word], our discovery of errors will be down ; and somebody then is either going to conclude, right, we have almost corrected, or secondly what are these blokes doing if they are not bringing in the money...” (MM4: p24).

Thus the tension between two forms of performance measurement and reporting is clear as the manager argues that good performance on *customer-focused dimension* may lead to poor performance on the *traditional compliance enforcement* based performance measurement.

HMCE is a public sector organisation, as was discussed in Chapter 4. Like other similar organisations it receives monetary resources from government to fulfil organisational aims and objectives. But despite having common attributes of public sector organisations, it has a few distinguishing features of its own. In terms of Fig 8.1 in Chapter 8, the most distinguishing feature of HMCE is the presence of strong reciprocity in accountability relationships. And consequently, many notions of the private sector performance frameworks are not so easily



applicable. For instance, the notion of *customer* is not well established, as was explained in chapter 8. Similarly what is the *service* that the department provides is also not well defined, as the recipients of the services view the HMCE as an organisation which tries to achieve its revenue targets. These contextual differences make the application of private sector inspired customer focus based performance measurement all the more difficult in the case of HMCE.

The issue of difficulty in applying well known performance frameworks to HMCE can further be analysed with the help of a generalised framework proposed by Carter (1991: p 89). The author suggests seven determinants of *difficulty* in conceptualising performance and hence designing adequate performance measures in the case of organisations. The framework is explained by the author by considering the examples of public and private sector organisations e.g. the Police and Supermarket<sup>88</sup>. The author argues that if an organisation is providing heterogeneous and complex services for which defining ‘outcomes’ is difficult, then designing adequate PIs is difficult for such organisations, irrespective of the fact that they are public sector or private sector organisation. The author argues that the higher an organisation is on the dimensions of *Accountability*, *Heterogeneity*, *Complexity* and *Uncertainty* the more difficult would it be to define performance in simple terms and thus hard to assess it.

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<sup>88</sup> The author enlists three most important determinants as *heterogeneity*, *complexity* and *uncertainty*. By the degree of *heterogeneity* the author means the number of different products or services provided by any organisation. The author believes that conceptualising and assessing the performance of a single-product organisation is less difficult than assessing that of a multi-product organisation. By the degree of *complexity* the author means the extent to which an organisation has to mobilise a number of different skills in order to deliver its services or produce its goods. Lastly, by the degree of *uncertainty* the author means the unclear causal relationship between means and ends.

In earlier chapters the historical origins and the range of functions performed by the HMCE were discussed which established that it is a very complex organisation. HMCE scores high on the dimensions of *Accountability*, *Heterogeneity*, *Complexity* and *Uncertainty* in terms of the framework proposed by Carter (1991). Its functions are quite diverse and range from simple tax collection to anti-smuggling activities, and lately, anti-terrorism activities as well. This makes HMCE quite a *heterogeneous* organisation. Similarly skills requirement range from legal, accounting and auditing to pure law enforcement and management. In terms of outcomes, tax revenue and tax gap minimisation are outcomes which are not entirely dependent upon the efforts of HMCE alone. Therefore, it is not surprising to find that conceptualising performance is not an easy task in the case of HMCE and the presence of *reciprocity* in accountability relationships makes a customer-focused performance measurement [e.g. SR (2000) PSA] difficult to work.

## **10.2 Influence of Private Sector Performance Frameworks**

The preceding discussion underscores the context of HMCE which is elaborated in terms of *organisational* and *accountability* complexity where the element of reciprocity in accountability relationships is an important distinguishing factor. Many authors (e.g. Mueller et al. 2004, Talbot, 2000) argue that the governments have been hastily adopting private sector models of performance measurement and management under the influence of NPM. Despite its different context, the HMCE also implemented the PSA related accounting reforms. But is there any direct evidence that the private sector models have influenced the PMS of HMCE? The mere fact that performance is measured and reported is not



significant since the use of performance indicators is not something which the public sector borrowed from the private sector (Williams, 2003). However when performance is approached by the public sector managers in terms of *drivers* and *determinants* of performance it can be termed as a visible impact of private sector performance measurement frameworks.

Fitzgerald et al. (1991) in their framework *RDF* classified measures into two types: relating to results (competitiveness, financial performance) and to determinants of those results (quality, flexibility, resource utilisation and innovation).

How can the PMS prescribed by the PSAs of SR 2000 and SR 2002 be interpreted with the help of results and determinants approach? In order to apply RDF, the first challenge is defining what is ‘result’ and what are ‘determinants’ in the case of HMCE? The definitions would depend upon the perspective of performance as viewed by different stakeholders. For instance, the tax managers would view revenue collection figures or tax gap reduction the ‘result’ and all other measures such as quality of service delivery, taxpayers’ satisfaction would be considered ‘determinants’. But if the RAF approach is taken, the perspective of taxpayers will be equally important. Therefore, the two triangular halves, compliance driven PMS and Public accountability driven PMS, will have their own results and determinants, independent of each other. In this paradigm of accountability relationships *compliance accounting* provides information to the resource provider, while *customer accounting* informs the taxpayers as to how well the tax authorities performed from their perspective. Hence in this approach, both compliance driven dimension and public accountability dimension of

performance will have their own *results* and *determinants*. It is possible that some determinants may be common to both dimensions but, importantly, it is equally probable that a positive determinant for one dimension may prove a negative determinant for the other.

<i>Dimension</i>	<i>Objective</i>	<i>Outcome Targets examples</i>	<i>Examples of PIs</i>
<b>Compliance</b>	<b>Results</b>		
	Right revenue at right time	Projected tax collection targets	Correct returns filed ( with a quantitative target)
		Extra revenue collection target	
	<b>Determinants</b>		
	Better IT enabled services	electronic returns filing	%age of services available and take up rates (with quantitative targets)
	Better advice provision	coverage through advice centres like National Advice Centre for VAT enquiries	service standards targets (common to all Central government departments)
	Taxpayers satisfaction	improvement in taxpayers level of satisfaction with the services provided by tax department	surveys conducted through private sector researchers
	Better resources utilisation	achieve productivity gains on annual basis	% savings by costs reduction without undermining services provision
<b>Public accountability</b>	<b>Results</b>		
	Compliance costs reduction	Reducing compliance costs to the minimum level	% reduction assessed through surveys
	Psychic costs reduction	Reducing complexity of tax laws	Simplified legislation through taxpayers surveys
	Taxpayers satisfaction	improvement in taxpayers' satisfaction with the services provided by department and conduct of tax officials	surveys conducted through private sector researchers
	<b>Determinants</b>		
	Better IT enabled services	electronic returns filing	%age of services available and take up rates (with quantitative targets)
	Better advice provision	coverage through advice centres like National Advice Centre for VAT enquiries	covered through service standards targets (common to all Central government departments)
	Trust based self assessment	-	-
	Reduced intrusion into affairs of compliant businesses	-	-

Table 10.2: SR (2000) PSA in the format of RDF and informed by RAF (adapted by the PhD author)



The SR 2000 PSA of HMCE can be re-examined for results and determinants, keeping the two competing perspectives of performance in mind, and the results are tabulated in Table 10.2. From the table it can be seen that some determinants like better IT enabled services, advice provision and taxpayers' satisfaction can be common to both dimensions of performance. However some determinants like reduced intrusion into affairs of businesses may improve perception of performance on public accountability dimension but it may result in possible evasion of taxes by opportunist businesses and thus lead to poorer performance on compliance dimension of performance. Similarly, efficiency gains can be achieved by shifting the burden of collecting taxes to the taxpayers which result in increasing the compliance costs (Sandford et al., 1981).

Thus in RAF approach there is recognition of the possibility of tension between the two aspects of performance<sup>89</sup>. In 2002 new PSA was introduced by HMCE as explained in chapter 9. It can be argued that the new PSA 2002, based upon 'tax gap' approach, brought the PMS much closer to the private sector styled RDF. If the design of PSA 2002 is examined, it is not difficult to identify the underlying assumption that the tax collectors and the tax payers are partners in achieving the common goal. It can be seen that in terms of RDF *customer accounting* is not juxtaposed in competition with the *compliance accounting* but instead is seen as a *determinant* of performance resulting in good *compliance results* i.e. 'positive success' (Brumbach, 1988: p 388). Financial performance in the case of HMCE is the achievement of *theoretical tax yield*. This result is measured by compliance

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<sup>89</sup> Since the Treasury Select Committee represents the interests of Government as a resource provider on one hand and taxpayers as citizens on the other, it can be seen as a broker to strike a fair trade-off between the competing interests of the two stakeholders of a tax system.

accounting related measures/PIs. Customer accounting related measures can then be viewed as measuring those drivers which help in achieving the desired final result of theoretical tax yield or minimising the tax gap. Thus *customer accounting* can be viewed as somewhat equivalent to *the determinants* of RDF or *the customer perspective* of the BSC. Arguably, the implied assumption here is that better customer focus would make the taxpayers more satisfied which would increase voluntary compliance and that in turn would lead to the achievement of final outcome, i.e. the theoretical tax yield. If the PSA 2002 of HMCE is recast in the form of RDF, it may look like the following table:

Category	Objective	Outcome Targets	Measures and PIs
Results:			
	Achieving theoretical tax yield	Projected tax collection targets	Revenue Collection Figures, Correct returns filed ( with a quantitative target)
		Extra revenue collection target	Extra revenue collected
Determinants			
	Better IT enabled services	increasing electronic returns filing	%age of services available and take up rates (with quantitative targets)
	Better advice provision	coverage through advice centres like National Advice Centre for VAT enquiries	Service standards targets (common to all Central government departments)
	Taxpayers satisfaction	improvement in taxpayers level of satisfaction with the services provided by tax department	Surveys conducted through private sector researchers
	Better resources utilisation	achieve productivity gains on annual basis	savings by costs reduction without undermining services provision

Table 10.3: The PSA 2002 in RDF format – adapted by the PhD author

In the RDF proposed by Fitzgerald et al (1991) determinants like innovation, flexibility and resource utilisation help a business entity achieve competitive edge which leads to better financial performance. One may argue that the tax



authorities are monopolies therefore the question of achieving competitive edge does not arise. However the new performance accounting system implemented through *Resource Accounting and Budgeting* (RAB) by the central government since 2001 creates a proxy market competition situation for all the government departments. An important government report claims that RAB would improve planning and controlling of spending and increase the incentive to manage resources more effectively (HM Treasury, 1998: p 10). Moreover, resources are tied up with performance targets in order to shift focus from inputs to outcomes (Likierman, 2001). In response to a question by a TSC member, the Chief Secretary of the Treasury replied:

“... as part of the Spending Review process, of course, there are negotiations with departments about resources going forward. At the same time, we are negotiating about the toughness of targets and the two are a joint exercise and obviously there are discussions with the Prime Minister as well” (TSC, 2003)

Therefore in order to receive funds from the Treasury, all government departments are in a state of competition. Their continued resources support would depend upon good performance with regards to achievement of performance targets and productivity gains. Therefore the efficiency determinant in RDF remains as valid in the case of HMCE as it is for private sector businesses.

The determinants like *Better IT enabled services*, *Better advice provision*, and *Taxpayers satisfaction* can be appreciated if it is understood that voluntary compliance by the taxpayers is the most important driver of performance for any tax administration. Customer-focused improvements encourage taxpayers comply with the tax laws voluntarily which in turn lead to good financial performance, i.e. increased tax revenue or as per jargon *reduction in tax gap*. The

overriding emphasis upon such enablers of good performance is also explicit from the following comments of a senior manager:

“... the e-programme is a very expensive programme, in as much as; there is a lot of government money going into that and over three year period and what the chairman was saying was, you know, this is the other area, that you are going to stand or fall on; you can deliver the strategy, you can deliver the e-programme, and similar to the strategy is very important to have articulated the e-programme in a way that has been sufficiently, I shall say, sufficiently compelling and persuasive to get ministers and treasury and the office of e-envoy to say yes we like what we see, we think we should invest in that, and that's major achievement we got that for and now the next stage, really beginning now is to, over the next three years, to deliver that, and, now what, it's important for the vat business is that first of all, it should lead to efficiency to the way we do things, it should lead to the efficiency to the way taxpayers do thing...” (SM1; p 12).

Four themes are noticeable above. First, IT development i.e. e-programme is as important as the overall strategy itself. Second, failure in e-programme amounts to failure in overall strategy implementation. Third, there are improved chances of getting greater funds from the resource provider, the Treasury, if they are convinced that the e-programme will lead to achievement of strategic objectives. Thus for the Treasury giving additional funds to HMCE is like making a prudent investment with the hope of cost savings (less cash outflows) and additional tax revenue (more cash inflows) in the near future. Fourth, the improved IT facilities to the taxpayers lead to reduction in compliance costs which improve voluntary compliance which in turn results in improved revenue collection by HMCE.

If the Results and Determinants approach is applied with insights drawn from the social exchange theory as expounded by Alford (2002), *voluntary compliance of tax laws by taxpayers* can be thought of as the desired result. The determinants for this result are the *perceptions of fairness and equity* in the minds of taxpayers. These perceptions can be measured through taxpayers' satisfaction surveys. *Customer focus* can therefore be viewed as the efforts made by the tax authorities to improve the taxpayers' perceptions of fairness and equity. This



fusing of RDF with social exchange theory resolves some of the difficulties associated with conceptualisation of private sector notions of *customers*, *customer-focus* and *service delivery*. The Principal is identified as the Government to which the tax administration is accountable under managerial accountability. The accounts take the form of PSA based performance measurement. The government as a Principal certainly has both powers of "incapacitation" or "deterrence" (Elster, 1999: 255), as HMCE depends on resources it gets from the Government. However the approach works as long as taxpayers are not treated as a stakeholder in their own right.

### **10.3 The Balanced Scorecard**

While reviewing the PSA based performance measurement framework of the New Labour government in Chapter 6, it was observed that the influence of Lynch and Cross (1991) in official publications was quite evident. In the previous section it was learnt that the latest PSA of HMCE is styled after *Results and Determinants Framework* of Fitzgerald et al. (1991). The review of official publications on accounting reforms in chapter 6 had also suggested that the influence of BSC, one of the most popular performance measurement frameworks popularised by Norton and Kaplan (1992), was also quite visible in the accounting reforms of the New Labour Government. In this section the role of BSC as a strategic policy instrument is briefly reviewed and then it is examined as to what extent this has been followed by the HMCE.

Kaplan and Norton (1996) suggest that the BSC helps an organisation introduce four new management processes that, separately and in combination, contribute

to linking long-term strategic objectives with short-term actions. The authors claim that the first process, *translating the vision*, helps managers build a consensus around the organisation's vision and strategy. The second process identified is *communicating and linking* which lets managers communicate their strategy up and down the organisation and link it to departmental and individual objectives. The scorecard gives managers a way of ensuring that all levels of the organisation understand the long-term strategy and that both departmental and individual objectives are aligned with it. The third process *business planning* enables companies to integrate their business and financial plans. The authors advocate that managers should use the ambitious goals set for balanced scorecard measures as the basis for allocating resources and setting priorities so that they are able to undertake and coordinate only those initiatives that move them toward their long-term strategic objectives. The fourth process, *feedback and learning*, helps in strategic learning as an organisation can monitor short-term results and modify strategies to reflect real-time learning.

It is clear from above description that BSC adopts a holistic view of performance management where performance is clearly understood and the meaning is shared across the board in an organisation. It can be argued that HMCE adopted the BSC styled outcomes based performance management system of PSA with some notable omissions. For instance, this PhD research found that the BSC's second process of *communicating and linking* had been inadequately addressed by HMCE while implementing major accounting changes. Though, the middle level managers interviewed were mostly aware of the emphasis on new strategic focus and reconceptualisation of performance in terms of plugging the tax gap, yet PSA and its objectives did not appear to be prominent in their discourse. Even



when PSA was specifically mentioned to them, they appeared not to be very familiar with the contents of this strategic document. Their concern was mostly with their own day to day official duties and related engagements. Hence their conceptualisation of performance was governed mostly by their own experiential knowledge and the operational level accounting routines such as performance agreements and reports<sup>90</sup>.

Like many other large organisations, HMCE is using email and intranet mainly for the purpose of communication with its personnel. This over reliance on IT based facilities has compromised the quality of communication, as one manager lamented:

“We don’t get that any more. It’s all on the Intranet and when you ask well where do I find out this, oh read it on the Intranet. And it assumes that you have got, I don’t know, an hour each day to sit and read it. If I read everything that was put on the Intranet every day, I’m not sure how long it would take me to do that (MM5: p21)”.

The ignorance of an operational level employee (OL1:12-13) about PSA was mentioned in Chapter 9. In fact, the officials were found too occupied with their own day to day activities to afford time for pursuing and understanding strategic level changes on their own. As one official remarked:

“... day to day official stationary going in trays; it gets in the way” (MM4: p12).

No organisational level effort was witnessed to inculcate new meaning of performance or other accounting changes into the mindsets of employees. Therefore, it was found that PSA was considered by the respondents to be a high

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<sup>90</sup> Romzek and Ingraham (2000) examine the unintended consequence of relying upon information technology as the only means of intra organisational communication. They observe that the speed of communications coupled with the casual attitude individuals take to email communications may increase opportunities for miscommunication.

level policy document which is only of concern to the policy people sitting in the HQs.<sup>91</sup>

It can therefore be argued that even though *revenue maximization* had been taken off the policy targets of HMCE in PSA 2000 and reported separately in a *Trust Statement*, it still remained the most important desired outcome for tax policy management. For instance, a senior manager explaining the newly adopted strategic approach said:

“....we are here to help reduce that gap and therefore all of our policies; everything we do in vat should be contributing to that so the strategy and the chancellor agreed to that and in the budget statement there is a commitment; there is first of all an acknowledgement that this is and also there is actually a commitment saying what the Customs and Excise is doing is focusing on reducing, not eliminating, because that’s impossible, reducing that gap and we have a commitment to reduce that gap....” (SM1: p8).

The main publication outlining the departmental strategy also makes a clear reference to this desired strategic outcome:

“The strategy is designed to reduce the size of the shortfall and produce more than £2 billion per year of additional revenue by 2005-06. This is the Government’s aim, but in line with its cautious approach to the public finances, and with the agreement of the National Audit Office (NAO), a lower estimate of the yield is being projected in the Pre-Budget Report public finance forecast” (HMCE, 2002e: executive summary).

Kaplan (2001) adapted the balanced scorecard to non-profit organisations by realizing the importance of mission objectives in the multidimensional framework. In this modified version both the resources providers and recipients of the organisational services have been placed at the same level below the mission of the organisation. Then follow the business processes and internal

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<sup>91</sup> The department did not provide any training or special directions to the middle or operational level employees. All such material was placed on the official intranet, which appeared not to have been read by majority of the respondents, as they were already hard pressed with their daily official routines.



learning perspectives. If the PSA of HMCE is compared with the balanced scorecard of Kaplan (2001) it can be seen that the emphasis on multi-dimensional nature of performance is also visible there.

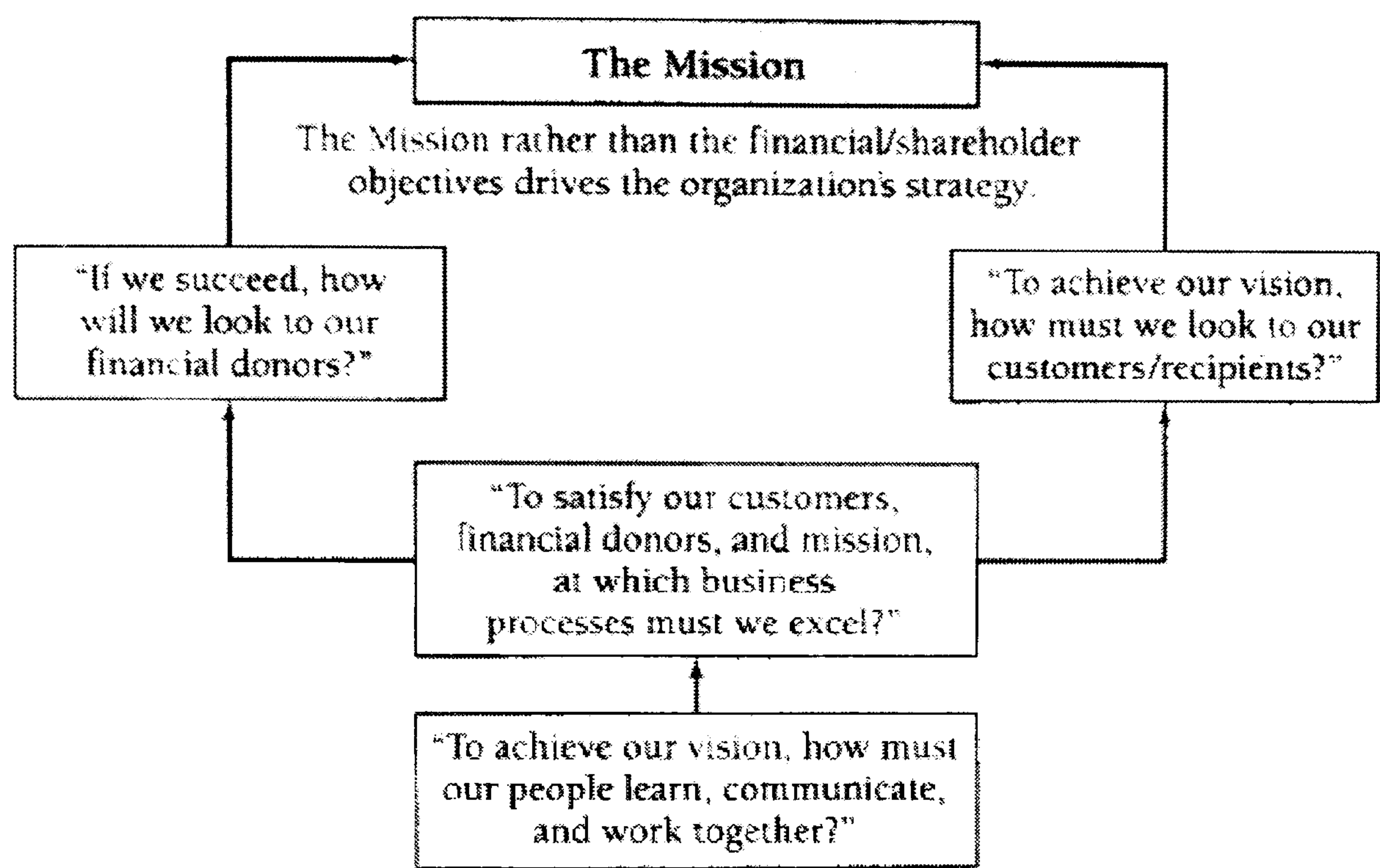


Fig 10.2: BSC for Non-profit organisations (Source: Kaplan, 2001: p 361)

By setting up policy targets for various aspects of performance like compliance, taxpayers satisfaction, and productivity the policy managers clearly made an effort to design a multidimensional performance framework. If the PSA of HMCE is viewed from BSC lens, it can be redesigned and presented as:

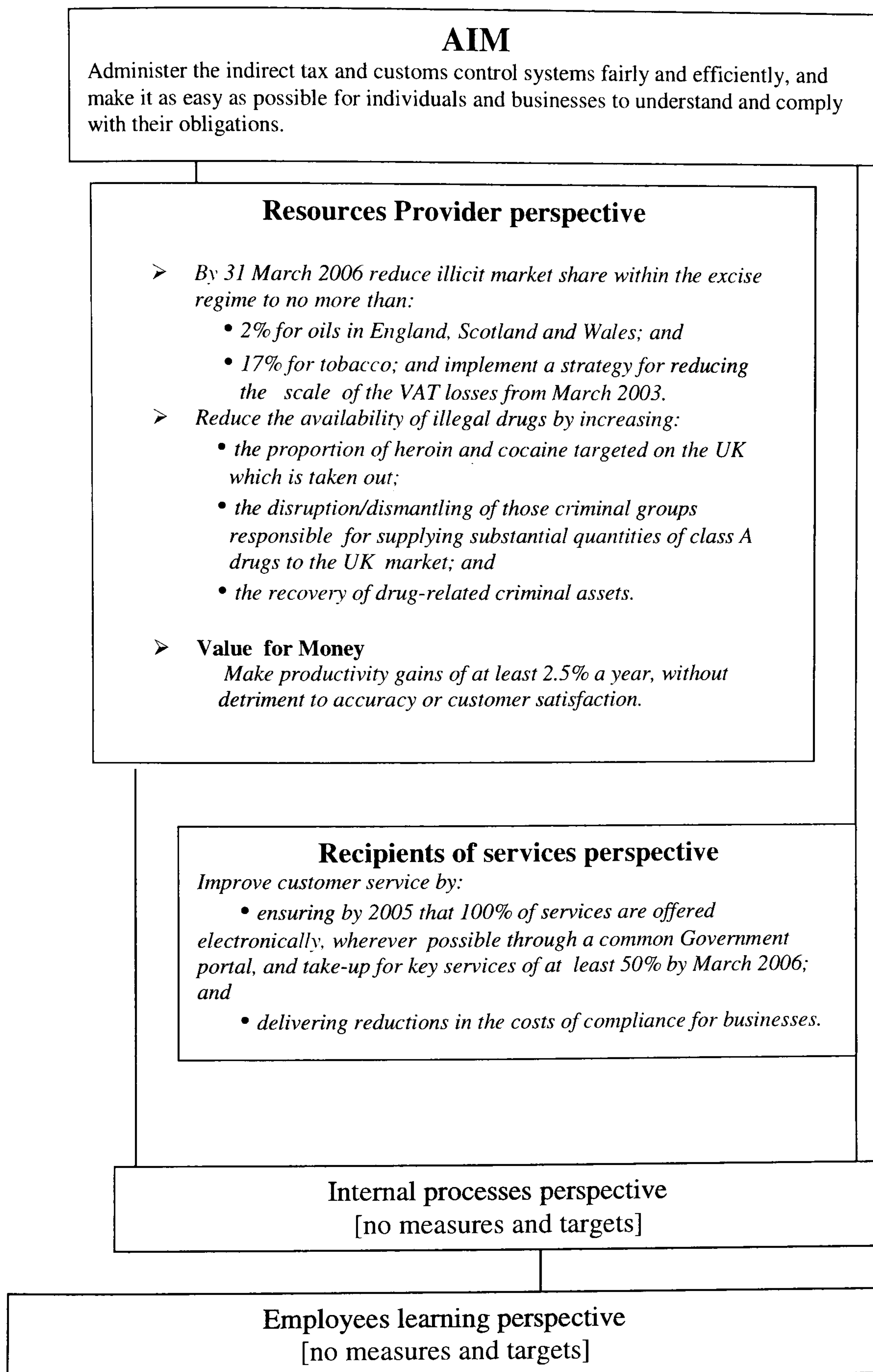


Fig 10.3: PSA 2002 in the form of BSC (adapted by the PhD author)

It can be seen that two perspectives of BSC, *the internal processes perspective* and *employees learning perspective* do not appear in the PSA. However this



should not necessarily lead to the conclusion that the HMCE management does not give importance to these drivers of performance. In fact, as already noted in earlier chapters, in the official discourse there has been a recurring emphasis upon modernization of IT systems used by the organisation. Similarly there are training courses available to different categories of employees. But as Nørreklit, (2000: 67) argues, the balanced scorecard views all perspectives of importance as equally important:

“The crux of the balanced scorecard is the linking together of the measures of the four areas in a causal chain which passes through all four perspectives”.

The authors of BSC have also underscored the need for including the indicators of performance drivers along with the outcome indicators in the scorecard:

“A scorecard should contain outcome measures and the performance drivers of those outcomes, linked together in cause and effect relationships” (Kaplan and Norton, 1996; p. 4) .

The PhD research found little evidence to suggest that the designers of PSA for HMCE had consciously adopted BSC or that the performance policy managers had pursued implementation of BSC as a policy target<sup>92</sup>. No clear references to adoption or adaptation of BSC were found either in the official publications or the discourse of the management of HMCE. For instance, the managers responsible for operational performance indicators and individual performance appraisals did not mention BSC in their replies to questions asked by the PhD

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<sup>92</sup> In stark contrast we do find such clear policy pronouncements in the case of Inland Revenue. For instance, the former IR chairman Mr Nick Montagu, delivering his speech as a foundation speaker at the Public Policy and Management Forum, Qinghua University, Beijing in January 2002, and explaining the public sector reforms with the help of IR, made a very specific reference to the balanced scorecard. Similarly the Swedish Tax Administration supplemented its Performance Measurement Model (PMM) with a balanced scorecard so that the top management could gain a broad view of performance through a limited number of key indicators reflecting central elements of the management plan. (OECD, 2001; p 46-47).

researcher regarding performance measurement within HMCE. A senior level manager (SM1: p 6) was categorically asked about BSC with reference to IR but even though he did stress the adoption of strategic focus approach as something new in the organisation he never mentioned BSC as the instrument for achieving the same. Thus in view of these evidences it can be concluded that HMCE has not considered adoption of BSC as the basis of its performance measurement framework.

A relatively new framework of performance measurement *Performance Prism*, proposed by Neely et al (2000), was mentioned in chapter 2. The framework demonstrates the way in which an organisation's results (stakeholder satisfaction) are a function of determinants (the other Prism facets). The authors thus broaden the scope of performance measurement by incorporating stakeholders approach into multi-dimensional framework. The PSA of HMCE does carry imprints of the stake holder approach as is visible in the prism performance framework. Examining the objectives and policy targets with performance indicators in the PSA, it can be argued that the resource provider (*The Treasury*), society at large and the tax payers are the identifiable stakeholders around whom the PSA framework of HMCE has been designed. However it does not follow the performance prism in terms of detailed articulation of the stakeholders and the relevant processes and their associated measures.



## **10.4 Limitations of Performance Measurement**

The literature on performance measurement also looks at the limitations of performance measurement as a tool of performance management. For instance, Smith, 1993 identifies the unintended consequences associated with performance measurement. This PhD study has already highlighted the difficulty of HMCE in reconciling the two competing PMS corresponding to reciprocal accountability relationships. In an earlier section *organisational* and *accountability* complexities were found to be the explanatory factors for the difficulty in implementing the NPM inspired customer-focused PMS. The PhD study identified some additional issues which are important for understanding the context of HMCE with regards to PMS:

### **10.4.1 Reporting Good Performance**

In terms of principal agent model of accountability the first and foremost purpose of measuring performance is to enable the principal decide whether the agent has utilised the resources in the most effective manner and that whether the desired duties performed well? In the case of HMCE it was found that the notion of performance was influenced mostly by the historically imprinted ethos of law enforcement. However since HMCE is a department reporting to the Treasury, any definition provided by the latter will have the force of authority. One such statement was found by PhD research in a conversation that took place between members of TSC and senior management of the Treasury department.

“Q2 Chairman: Thank you very much. The focus for our session this afternoon is the departmental report. The report has a foreword by the Chancellor which refers to the government making progress, but I cannot find anywhere in the 85 pages any summary of the Treasury's own performance. This is an 85-page document costing £19, I think. Why is there no summary showing us how well the Treasury has done?”

Mr O'Donnell: May I ask what you mean? I see the Treasury's performance in terms of how well we are delivering on our objectives. What you get in terms of delivery is in terms of how we are doing against our Public Service Agreement (PSA) target. In terms of how the Treasury is doing as an institution, as a department, is that what you mean?

Q3 Chairman: No, I should like to stick with performance first. Is it simply measured against the targets?

Mr O'Donnell: Absolutely” (TSC, 2003).

Since Treasury department is the owner and enforcer of PSA framework, the unequivocal answer in the above excerpt establishes that the official definition of *performance* is achievement of targets set out in the PSA. Therefore, in the case of HMCE, organisational performance would also mean achievement of targets as set out in its PSA. Applying this definition of performance, the PhD research made an interesting finding which is explained below.

From the resource accounts in the Annual Report, 2001 (HMCE, 2001a), the targets met or not met are summarized and presented in table 10.4 below:

Policy Targets	PIs Met	PIs Not met	PIs discontinued	% Met of total
1 Compliance	2	2	0	50%
2 Cigarettes	3	1	1	60%
3 Drugs	5	0	0	100%
4 Int Trade	1	2	2	20%
5 E-services	2	1	0	66%
6 Compliance costs	0	1	1	0%
7 Productivity gains	1	1	0	50%
8 Customer service	0	1	0	0%

Table 10.4: A summary of targets met or not met

In the table above column 1 is the policy targets, while columns 2 and 3 represent how many of the PIs specified under a policy target were met or not met. Some of the PIs were discontinued due to some organisational changes or irrelevance and listed in Column 4. The last column provides percentage of PIs met, thus a measure of performance. If all PIs are considered the final performance picture is given by the following table 10.5.



Total PIs	Met	Not Met	Discontinued	% Met
28	14	10	4	50%

Table 10.5: Performance as achievement of targets

It therefore follows that as per the Treasury’s definition of performance, HMCE had a 50% achievement of targets on the whole. The picture is even worse, if the policy targets are seen in terms of their relative importance. If *Compliance*, *Customer satisfaction* and *productivity* are identified as the three major outcomes areas, the department did not meet targets in the *customer satisfaction* and *productivity* areas. Non-achievement hence rises to almost 66%. So should we conclude that performance measurement shows that the department achieved 33% of performance level expected of it? In any private sector organisation, this should have caused much unrest. But oblivious to the numbers, the *Spring* and *Annual Reports* of HMCE in 2001 and 2002 only highlight achievements in traditional fields of revenue collections and law enforcement. The point emerging from this analysis is that the PMS is failing in its basic purpose. It is not telling its users in clear terms ‘how well the organisation is doing? This will have consequences on accountability system as the basic purpose of performance measurement is to operationalise the accountability relationships.

#### 10.4.2 Operationalising an Outcome Target

The difficulty in reducing an outcome target to an operational target is well documented (Likierman, 1993; Carter, 1991)<sup>93</sup>. In chapter 6 the confessions of

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<sup>93</sup> A survey by NAO shows that public sector organisations face the greatest challenges in dealing with issues of ownership and reward for achieving targets, with lesser but still common challenges in influencing service providers’ priorities and integrating PSA targets into normal planning activity (NAO, 2001)

the top management of HMCE before the TSC established that the efforts of HMCE to operationalise outcome targets of SR (2000) PSA failed as these produced somewhat embarrassing final results. One such target was that of *productivity*. In order to avoid the same results in the future, special care was taken to redefine the *productivity* measure in the new PSA announced in 2002. Interestingly no calculation method for productivity gain was provided in the *Technical Notes* for almost a year. It seems that after many internal deliberations the measure was finally recast in such a way so that positive outcome could be reported on this dimension of performance as well. It is now measured in terms of *staff years reduction* and *procurement savings*. Not only was productivity measure fine tuned to avoid any nasty surprises, other performance measures that were sitting uncomfortably in the earlier PSA were also sidelined and relegated. These included *Customer Satisfaction* as measured by *Customer Satisfaction Index* (CSI) and *compliance costs reduction*, which do not appear as the main policy targets in the new PSA. Not surprisingly, in the latest *Annual Report*, all measures including productivity are positive.

#### **10.4.3 Ease of Comprehension**

Since the purpose of performance measurement is to enable the principal make an informed judgement on the performance of the agent, it is important that the principal should be able to read and understand the *accounts* without much difficulty. The review of PSA framework establishes that the format of accounts is not easily understandable to a lay person. This is evident from the fact that even the chief secretary to the Treasury (the owners of the PSA framework) had



difficulty in explaining various terms used in the performance reports to the members of TSC.

“Forgive me, but it is clearly not transparent enough when an intelligent colleague on this Select Committee pointed out "*on track*" and "*ongoing*" and you had great difficulty explaining, you, an intelligent man, what on earth it was about...(TSC, 2003).

The taxpayers were identified as the *principal* under public accountability relationship to the HMCE in RAF. In view of the difficulty in reading and understanding the performance measurement and reporting of PSA, it can be argued that the taxpayers will not find performance reporting of HMCE an effective instrument of accountability.

#### **10.4.4 Fragmented Performance Measurement**

The private sector frameworks advocate a holistic view of performance measurement where performance is measured in the form of a cascading pyramid. The PMS of HMCE was found to be quite fragmented. While PSA is the high level performance framework, the department also reports performance for *National Standards* and *Diversity*. Similarly, many operational level performance sheets (inherited from pre-PSA era) are in use in different field formations. These stand alone performance reports are however not integrated into the PSA framework; therefore it is not clear how these various performance regimes are prioritised at the organisational level.

#### **10.4.5 Lack of Verifiability**

The *accounting data* is expected to play its role as an instrument of accountability only if the data is of very high quality and externally verifiable. The performance reporting in HMCE suffers from the problem of lack of

verifiability. This problem is inherent in the PSA framework on the whole. For instance a special report of Public Administration Committee (PAC, 2003) reviews the limitations of target setting suggested that there should be external verification of targets being met or not met. Same concerns are expressed by the Treasury Select Committee in one of its sessions when the Treasury's top management defended the quality of data:

"I come back to the point. Do you think there is no scope at all for getting the NAO to come in and externally verify this data and make it more transparent? Do you think the public is happy with what you are producing or do you actually think there is something in what Parliament and some parts of Parliament are saying, which is that we should get an external verifier in? Do you not think there are any grounds for that at all? Is that what you are saying: it is so great that there is no room for improvement?" (TSC, 2003: Q55)

The issue of verifiability is all the more important in the case of HMCE as the main outcome measure '*tax gap*' is a hypothetical measure. Due to this fact, and recalling the difficulties faced by the department in measuring and reporting its performance in SR (2000) PSA, the need for external verification can not therefore be overemphasised.

#### **10.4.6 Separation of Policy and Operational Measures**

The HMCE reports to the Treasury and hence it can be assumed that the Treasury has the policy function while HMCE is obliged to carry out operational functions. But the picture is blurred if the Annual Reports of both HMCE and the Treasury are examined. It is found that the performance of HMCE is not well knit with any of the PSA objectives and policy targets of the Treasury. In fact out of total of 10 policy targets of the Treasury's PSA (Annex 10.1), only one target,



i.e. Policy target No 8 appearing under objective 7 has any taxation content<sup>94</sup>. As can be seen the child poverty reduction target shared with DWP in no way reflects the performance of HMCE which is a subordinate department of the Treasury. One may argue that the tax gap reduction related revenue collection by HMCE helps the Treasury achieve its macroeconomic related objectives such as fiscal balance measured by targets such as net debt etc. However, the PMSs do not provide any information as to what contribution is made by HMCE towards the performance of its parent department, the Treasury. Therefore, the accountability relationships between the principal (the Treasury) and agent (HMCE) do not seem to be cemented by the linkages of PMSs. This finding of the PhD research was substantiated by the O'Donnell report (which proposed merger of HMCE and IR) as it cites separation of policy and implementation as one of the key objectives of the merger.

“a Framework Document setting out who is accountable to whom, for what, in the new department, should be published. The Framework will be an opportunity for Ministers to set out long-term principles to govern the work of the department” (HM Treasury, 2004: p 12)

Whether the new department will be able to achieve the desired level of separation between policy and implementation and measure success by adequate PIs is a question which can be answered by a future research conducted in a few years time.

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<sup>94</sup> **Objective VII:** promote a fair and efficient tax and benefit system with incentives to work, save and invest.

8. Reduce the number of children in low-income households by at least a quarter by 2004, as a contribution towards the broader target of halving child poverty by 2010 and eradicating it by 2020. Joint target with DWP

#### **10.4.7 Performance Measurement as a Planning and Control Tool**

Planning and control are the foundations of any managerial system (Drury, 2000: p 6).<sup>95</sup> Three levels of control in the form of a pyramid: i.e. *strategic*, *management* and *operational*, were identified by Anthony in his seminal work in 1965 (Anthony, 1989: 11). It has been argued by many management accounting authors that the presence of an adequate rewards and penalties system is essential for effective working of a control system. For instance, Otley (2003: 312) argues that the actual functioning of control systems can best be judged from rewards and their distribution inside the organisation. Similarly, applying Otley (1987)'s framework of performance management, Moon and Fitzgerald (1996: 446) contend that an adequately designed system of rewards and penalties for good or bad performance at both individual and organisational level is essential for ensuring accountability and control. However in reality the functionality of a rewards system depends upon the nature of activities performed by an organisation and the degree to which the desired outcomes are related to *controllability* (Ghosh and Lusch, 2000).

From the replies of interviewees it could be gathered that the rewards system was not well developed in the case of HMCE. This is not to suggest that the management has been less thoughtful about its performance management system. Arguably, the organisational context of HMCE constrains the application of a

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<sup>95</sup> Drury reminds that Control is a word with 57 varieties of meaning ranging from 'dominate' through to 'feedback'. In managerial sense, the author refers to a range of possibilities, ranging from the domination of the management class over the workers (at the Marxist end of the spectrum) through to the adaptation of organisational activities to meet environmental exigencies (from a systems theory approach). *Planning* is defined as the design of a desired future and of effective ways of bringing it about, while *Control* can be defined as the process of ensuring that a firm's activities conform to its plan and that its objectives are achieved (Ackoff, 1981).



private sector performance management model. Otley (2001) also cautions against a single universal design of rewards as cultural differences are of great significance. This is not only true for country specific cultural differences but also applicable to organisational level cultural differences. As one manager in HMCE argues that linking reward system to achievement of targets maybe appropriate for organisations where final outputs are quantifiable and standardized, but very difficult to situations where final outputs are not clearly defined or controllable. One manager explained the systemic constraints in the following manner:

“Well I don’t think we’re any different from any other Department or any other sectors that deals with something that’s not a tangible production...if you have numerical measures you must have qualitative as well, because it’s no good producing a thousand cups if they’re all chipped, so you must have qualitative side, and then we have the behavioural side also. But then it’s still very difficult at times to distinguish one person’s performance from another” (MM6:p 5).

Tax collection is a process whose final output, i.e. tax revenue, is dependent upon many factors which are beyond HMCE managers’ control, as explicitly expressed by one manager:

“... that is right because, you know, to some extent the outcome is only partly with in your control” (MM2: p 4)

Due to these systemic constraints, the desired ‘*accountingisation*’ can play a limited role in performance management of HMCE. Consequently, the use of targets-based performance management model, operationalised through PSAs, in a cascading manner, proved very difficult. Though the cascading model had been prescribed by the Government in its *Business Planning Model* (HM Treasury, 2001a: p 6), the HMCE managers were almost unanimous in considering quantitative targets as inappropriate. The following reply makes it clear:

“they are not assigned quantitative targets except in the case of the highest risk group that we are dealing with which is trader group 6, the only targets we have there is to ensure we use the time allocation that is given to us but we have no targets in terms of results from them...so we have these figures to go for but I think your question is that each individual has individual targets. The answer is no. [adding] Union does not agree to that” .(MM2).

The historical review of the organisation in chapter 4 and the categories of functions performed established the highly complex and heterogeneous nature of the outcomes desired by HMCE. It is therefore not surprising to find that while achievement of outcome targets is appreciated at managerial and organisational levels, there is no system of rewards and penalties. An excerpt from an interview makes it clear where the interviewee is asked about likely consequences of not achieving targets:

“MM4: there wouldn’t be repercussions exactly; it’s just that if a division were to fail to meet its targets its obliged to say why, to provide some sort of explanation as to why this or that target has not been met  
HS: so if the explanation is satisfactory then its o.k.; and if not then some penalties maybe imposed, so what are the penalties?  
MM4: there are no penalties  
HS: and what are the rewards if you achieve the targets?  
MM4: none”

The research found that the traditional performance appraisal (PA) system was still used for evaluating individual performance in HMCE. The problems associated with PA system are well recorded in HRM and applied psychology literature (e.g. Bowman, 1999; Fried et al, 1992): At the time of interviews, the PA process had been simplified, with the size of the standard appraisal form reduced from ten to two pages and more emphasis placed on regular face to face feedback from managers (TSC, 2001: para 1.3). It was however found that the employees were still not very satisfied with the PA system, believing it to be too subjective. The interviewees had concerns about the box division system whereby the individual was placed in good, effective or less effective boxes.



Many expressed their misgivings about the widely held suspicion that the centre wanted placing 10% of the employees in the less effective box.

HMCE was found to operate a performance related bonus pay system. Two interviewees from HRM team, at HMCE's London Head Quarters, in their reply specifically mentioned bonus pay system as a tool of performance management. However the PhD researcher had already discussed the issue with a few line managers who had declared them to be of no impact for practical reasons. When the HRM interviewees were confronted with those non-conformist remarks, they smiled and had to admit with approving body language like nodding that in practice effectiveness of such official recipes is limited.

At the organisational level, however it can be contended that HMCE would consider the attainment of its targets important because there is an element of competition involved. Under the new *Resource Accounting and Budgeting* system all the departments compete for allocation of funds. As argued earlier in this chapter, the likelihood of better funding would be increased if a department demonstrates good performance in terms of meeting PSA targets. Therefore reward for good performance would be continuation of or increase in funding while the penalty would be the opposite of that. This is also evident from the former chairman's reply to TSC:

"I have to say that on each one, as we have introduced the tobacco strategy, the oil strategy and the VAT strategy, in every case the Government have badged resources to these new strategies, so I have no problem at all with that. The issue really is, should an organisation of our sort, which is a large organisation with many processing functions, also be able to generate year-on-year cost reductions and efficiencies, to which the answer is also "yes". (TSC, 2002b: Q37)

The distaste of professionals for statistical targets is well documented (e.g. Broadbent and Laughlin, 1998). Some managers of HMCE were also candid in their lack of enthusiasm for using quantitative targets for the purpose of performance management. For instance, one manager dismissed the whole system as ‘number game’

“...At the moment as it is, I understand, the targets are being set probably at director level, advised by their advisers, whoever they may be, all the policy people. I am still waiting to hear what’s happening on the VAT side of things. I’ve certainly been involved in them, I’ve said that I don’t agree with the numbers game...” (MM5: p 24).

At the official level such discomfort with ‘accountingisation’ is, however, less noticeable. Those associated with the policy analysis wing in the HQs do use accounting information for the purpose of feed-forward control. Explaining the usefulness of accounting information, one manager explained the manner in which the performance related information is utilized:

“Yes, and out from that then the Director and his Regional Heads will have what’s called the traffic light system which has got all our measures and all our targets, and you know green if we’re all right, amber if we need to worry about it, red if we need to panic” (MM6: p 13 ).

From the above quote it can be seen that performance measurement is used as a ‘thermometer’<sup>96</sup>, a warning system.

A senior manager at HQs (SM1: p9) explained the use of performance data for exercising feed-forward control. According to the interviewee if resources were used in one region in strategically less important areas, he would inform the concerned Director along with remedial options, though the final decision was taken by the Director. Thus the information data is monitored by a dedicated

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<sup>96</sup> Boukaert (1993: 12) and Hirschmann (2002: 239) debate whether performance measurement is more like a sauna which gives out heat rather than a thermometer which only measures heat.



team which advises the Decision makers on more efficient utilization of resources for achievement of strategic objectives. Neely et al (1997) stress the system of generating useful performance data as the most important element of a PMS. However, the process of generation of useful accounting data in HMCE is itself marred by problems, as evident from the following remarks of a manager:

“But it has been troublesome pulling all that information together, and certainly at an operational level staff get frustrated that they’re constantly asked for more data by several sources. But a lot of that has to do with the fact that we have some Departmental systems which are creaking at the seams, and those that that issue is being addressed, but it takes a lot of money to address those for a long time” (MM6: p 13)

Even NAO expressed its concerns about lack of uniformity regarding generation of useful data:

“... at present there is no central performance reporting within the Business Services and Taxes Division, bringing together results for Large Business Group and Regional Business Services on a comparable basis. Both groups require their own unique reporting systems given their distinct business priorities” (NAO, 2003a: p 14).

Therefore, it can be concluded that in the case of HMCE management accounting is used for planning purpose, as evidenced by PSA, SDA and Departmental Plans. However systemic constraints limit the effective use of accounting information for the purpose of control, though it is partly used for feed-forward control.

The empirical analysis of performance measures used during 1997-2002 suggested that accounting data was used for enhancement of accountability in its multidimensional meaning. However the discourse of employees and the adoption of tax gap based performance measurement suggest that performance measurement has limited success in enhancing multidimensional form of accountability. Thus it can be argued that in HMCE performance measurement

has a well defined planning role but little evidence was found for enhancement of control and accountability.

### **10.5 Conclusion**

In the previous chapter, evidence was presented to establish that the accounting changes, such as PSA 2000, failed to shift focus from the traditional form of accountability relationships to the new NPM inspired accountability relationships. In this chapter explanatory factors for this failure were analysed. In terms of institutional theory it can be argued that the context of HMCE made it not suitable for implementation of the public sector wide PSA reforms of SR (2000). The HMCE, therefore, resorted to the response strategy of *manipulation* (Oliver, 1991) and *re-orientation* (Laughlin, 1995). It was argued that the PSA measures were recast so that the compliance based measures regain dominance over the competing public accountability based measures of performance. In addition to this generic explanation of institutional theory, other organisational specific reasons were also explored. While reviewing the PMS of HMCE a few other issues were also identified. The PSA 2000 and PSA 2002 were analysed with the help of RDF, social exchange theory and RAF, which was developed in Chapter 8. It was found that the private sector performance measurement models had influenced the PMS of HMCE. However, the influence is only implicit, and not a result of conscious adoption of any particular PMS e.g. BSC. It can be argued that though the PMS in prescribed by PSA 2000 and PSA 2002 was tailored according to the private sector models but the contextual ground realities made the private sector models limited in their use and effect.



## **Findings and Conclusions**

### **Introduction**

The PhD thesis set itself the research question of investigating the influence of NPM on a tax administration's accountability system, as operationalised by performance measurement. It desired to address the calls made by accounting scholars to carry out case studies in new research sites to improve our understanding of the process of accounting changes. Such case studies also improve our understanding of the change management ability of accounting changes with the help of the evidence generated by such case studies. In the previous chapters a study of the 1997-2003 period was carried out with the help of insights drawn from stakeholder theory, principal-agent model, institutional theory and the private sector models of performance measurement such as RDF and BSC. In this chapter findings of the study are brought together and conclusions are made with regards to the main research question of this PhD.

### **11.1 A Review of the Chapters**

Before the final conclusions towards the research question are drawn, the main points of the previous ten chapters are first reviewed so that the findings are brought together and final conclusions drawn.

In Chapter 1 the research area of this PhD study was introduced and motivation for the research topic explained. It was noted that despite the importance of tax authorities as public sector organisations they had largely remained very little researched (Tomkins et al. 2001). Since 1997-2002 was a period of major accounting changes in the public sector, the case study of HMCE provided an opportunity to analyse the pathways of accounting changes and to know as to what degree did they modify the accountability relationships. In chapter 2 important themes of relevant literature were reviewed with three main purposes. First, it helped in identifying important themes of NPM literature to set up the context in which the research had to be done. Second, it helped in identifying the theoretical underpinnings of the analytical tools used in the subsequent chapters and third, it also helped in spotting the obvious gaps in the literature so that the research could contribute towards filling those gaps.

In chapter 3 the case study method of research was justified as the most adequate method for this kind of research. The main research question and a few schematic questions were also formulated in the chapter. The chapter also identified primary and secondary sources of the PhD research. In chapter four the case study organisation was introduced and its historical origins were traced. This historical analysis helped in identifying the organisational ethos of the little researched organisation as many institutional theorists (e.g. Stinchcombe, 1965) argue that organisations formed at one time typically have a social structure which gets *imprinted* on the organisational psyche. The chapter also explained the existing structure and working of HMCE.



In chapter 5 a framework of categorising the PMS of tax authorities was proposed. Three examples of PMS of tax authorities were examined and it was found that the traditional emphasis on revenue collection/compliance varied in each case. While in one, i.e. CBR of Pakistan, performance was measured and reported solely on the basis of revenue collection figures, in Swedish Tax Authority, performance was measured and reported with greater sophistication; with the help of multidimensional outcomes, *productivity, quality and effectiveness*. The actual examples of how PIs are used differently by tax authorities helped in proposing a framework for categorising PMS of tax authorities. According to this framework, all PMSs of tax authorities lie on a line starting from the traditional form (where revenue raised and compliance enforcement defines performance) to the outcomes-based multi dimensional PMS. In between the two extremes are PMS where in addition to traditional revenue collection figures, some behavioural aspects are also measured and reported. The pre-PSA format of performance reporting of HMCE is analysed and cited as an example of a PMS where performance is mainly reported in terms of resources providers' concerns (i.e. revenue collection/ enforcement activities and productivity), however a few behaviour related PIs are also included to show that the organisation is not just vying for 'results' but rather for 'positive success' (Brumbach, 1988).

In chapter 6 the external environment of the HMCE was scanned. It was concluded that the institutional pressures emanated from the norms setting external environment, (such as other tax authorities in OECD countries), and the political environment (such as central government policies). It can be argued that in terms of NIS these normative and coercive pressures compelled HMCE to

move its PMS to one in which performance is measured and reported on the basis of multidimensional outcomes.

In chapter 7 the adoption of new PSA framework of SR (2000) was discussed. Due to the fact that equal importance had been given to both compliance and customer-focus in PSA 2000, it was positioned near point C of the figure. It was seen that the PSA created tensions between two competing forms of accountabilities which were operationalised by potentially competing forms of performance indicators. The private sector PMS related notions such as ‘customers’, ‘customer-focus’, ‘customer satisfaction’ and ‘customer-focused accountability’ were foreign to the ethos of HMCE. The broad brush approach of PSA required HMCE to redesign its PMS on the basis of these undeveloped notions which resulted in tensions between the traditional and NPM inspired customer-focused performance measures.

The analysis led to chapter 8 where a simplified framework of interaction of accountabilities in tax authorities was proposed in which *reciprocity of accountabilities* had the central importance. The framework captures the tensions between competing traditional and public/political accountabilities observed in the analysis of earlier chapters. It was stated that the tax authorities (the Board) are accountable to the tax payers in terms of political/public accountability, while the taxpayers are accountable to the tax authorities for tax liability in terms of legal accountability. The two forms of accountability relationships are operationalised by potentially competing performance measures/Pis. A multi-dimensional notion of performance is one which is based on information for both



resources provider and taxpayers to assess how well did the tax authorities meet their respective demands and expectations.

In chapter 9, three separate sources of evidence were examined with a view to achieve triangulation of data. First, the latest version of PSA framework i.e. of 2002 was analysed and it was contended that the apparent tension between the competing forms of accountabilities encountered in the earlier version of PSA was dealt with by the response strategy of *manipulation* and *reorientation* (Laughlin, 1991; Oliver, 1991). It was argued that the new version was based on the tax gap reduction approach which ensured that the traditional form of accountability remained dominant. Second, the discourse of personnel of HMCE and third, the merger of HMCE with IR were also presented as further evidence to substantiate the conclusion that the NPM inspired customer-focused accounting changes failed in achieving the desired effects.

In chapter 10, explanatory factors for the failure of first round of accounting changes, are analysed. It was found that organisational and accountability complexities did not make HMCE a very suitable organisation for the kind of accounting reforms that were hastily implemented. The coerced adoption of private sector styled performance measurement frameworks was made problematic by host of ground realities identified in the chapter. Now in this chapter the analytical gains of the previous chapters are put together so that the main research question is answered. The conclusions are grouped under three headings. First, the claims of NPM identified in chapter 2 are revisited with a view to ascertaining their validity in the light of evidence generated by this PhD research. Second, the RAF developed in chapter 8 is briefly reviewed and its

importance highlighted. Third, conclusions are drawn with respect to the more generic debate on the role of accounting as a force of change.

## **11.2 NPM and Tax Administration**

In chapter 2 the impact of NPM upon the public sector organisations was discussed. Four interrelated themes of NPM literature were identified which were:

1. Viewing the existing public sector management inefficient it advocates adoption of private sector styled managerial practices so that it can be made efficient.
2. Unlike traditional public administration, performance is measured and reported on the basis of end results or outcomes. This is in contrast to the traditional public administration where performance was defined in terms of following the rules.
3. There is an emphasis on the need for greater accountability of the managers where accountability is defined in terms of final outcomes. Thus managers are not just accountable for economy or limiting corruption, waste and incompetence but also whether they were able to achieve the outcomes for which resources were provided.
4. And there is more strategic place for performance measurement as it is considered an instrument of accountability as defined in theme 3.

Remaining attentive to these claims of NPM with respect to use of performance measurement for enhancing accountability, the main findings of the research are summarised next:



1. The influence of NPM inspired accounting changes was visible in the case of HMCE. This finding was anticipated as HMCE, being a central government department, had to adopt the PSA framework based new PMS. There is one important distinction, however, in the case of HMCE. Many other tax authorities which adopted NPM styled PMSs do make specific references to the private sector popular frameworks such as Balanced Scorecard<sup>97</sup>. No such references are made to the private sector frameworks either in the official publications of HMCE or in the discourse of senior management of the HMCE. The private PMS frameworks are, therefore, implied in the PSA versions adopted by HMCE. This explains why some important elements of the Balanced Scorecard are missing as identified in chapter 10.
2. The PSA framework does suggest that the organisational performance of HMCE had been redefined in terms of desired outcomes. Initially the pre-PSA measures and performance indicators were recast as outputs in the first PSA adopted in 1998. The PSA of SR (2000) can be seen as a major breakthrough as for the first time the traditional measures of performance, i.e. revenue collection figures were relegated to secondary importance as they were no longer part of the high level PSA measures. Also customer-focused measures were included such as taxpayers' satisfaction and compliance costs reduction in the PSA. These measures were also made

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<sup>97</sup> Earlier examples were cited of the Swedish Tax Authority and Inland Revenue of U.K which make clear references to the Balanced Scorecard when explaining the performance measurement changes.

part of the productivity measure. In the latest form of PSA, i.e. PSA 2002, the outcome is termed as tax gap reduction. So the effect of NPM in redefining performance as achieving *outcomes* is quite evident in the case of HMCE. However, in SR 2000 outcomes were more customer-focused as opposed to PSA 2002, where the outcomes are defined in terms of revenue collections efforts, thus more closely tied in to the traditional outputs.

3. The NPM's strong advocacy for using performance measurement is based on the assumption that this would lead to greater accountability which would in turn result in improved performance. It is this aspect of NPM which is of special interest in the case of HMCE. The causal relationship between accountability and performance is not so neatly linked as assumed by the NPM defined models of performance measurement. Due to reciprocity in formal accountability relationships two sets of potentially competing accountability relationships were found in the case of HMCE. The table 11.1 summarises all the performance measures and indicators appearing in the performance reports of HMCE during the period of analysis i.e. 1997-2003. After closely inspecting the measures/Pis they were grouped into four categories as *compliance*, *customer*, *efficiency* and *other measures*<sup>98</sup>.

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<sup>98</sup> The empirical analysis found that the measures could be categorized along four major classes. Following Fitzgerald et al (2004)'s typology, **Compliance Accounting measures** refer to the targets which may appear under different headings but essentially aim to enforce revenue laws and regulations. and thereby achieve the aim of maximising revenue receipts and minimising activities like smuggling and drug trafficking. **Customer Accounting measures** refer to activities which make the department accountable to the taxpayers. If the measures relate to activities which aim to improve service delivery, e.g., IT based services, making prompt replies etc, they are classified as *service delivery measures*, while those which measure the feedback of the users of the services, they are categorised as *Users Feedback measures*. The broad category



	Compliance Accounting			HR/ Efficiency	Customer Accounting		Other	Total
	Compliance	Anti -evasion & anti-crime	Tax revenue		Service Delivery	feed- back		
Next Steps	25	20	3	6	10		15	79
PSA 1998	0	12	2	6	12	1	23	56
PSA 2000	8	9	2	30	11	5	2	67
PSA 2002	-	7	-	1	4	-	-	12

Table 11.1: Category wise distribution of Performance Measures/PIs

No	Measures Category	% of total measures			
		<i>Next Steps</i>	<i>PSA 98</i>	<i>PSA2000</i>	<i>PSA2002</i>
1	Compliance Accounting Measures	61	25	28	58
2	Customer Accounting Measures	13	23	24	33
3	Operational/HR/ Efficiency related measures	7	11	45	8
4	Other measures	19	41	3	0

Table 11.2: Percentage wise distribution of Performance Measures/PIs

It can be seen from table 11.2 that performance reporting in *Next Steps* period was heavily *compliance accounting* focused as 61% of the total measures/PIs pertained to compliance while 13 % related to *customer accounting*. Thus it can be argued that it was a compliance driven accountability framework. With the advent of PSA framework in 1988, some sort of balance was tried to be achieved between the two competing accountabilities, as 25% and 23% of total number of measures belonged to the traditional compliance based and the newer customer-focused accountability relationships. But the real impact was felt in the SR (2000) PSA when the most important traditional measure

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of **Operational/HR/Efficiency measures** refer to targets which in essence aim to improving organisational efficiency by better management of human and physical resources. There were many measures which did not belong to these three broad categories and were thus grouped as **Other measures**. These pertain to functions which are not the core functions but are of ancillary nature, e.g. production of statistics, provision of advice or some time bound targets relating to preparation of strategy and plans.

of performance i.e. revenue collection was relegated to the trust statement while customer satisfaction was made one of the highest level performance measures. The emphasis, as a result, shifted in favour of PMS based on the newer form of accountability.

4. The tensions created by the two competing sets of measures based on two sets of accountabilities were ultimately resolved by the HMCE by resorting to the tax gap minimisation based PSA in 2002. Not only the proportion of number of measures relating to the traditional form of accountability regained dominance (58% of compliance accounting measures as against 33% of customer accounting measures), but the problematic measures such as taxpayers' satisfaction were also altogether removed from PSA framework. Thus the PMS based on accountability relationships is again a compliance driven one.
5. In the private sector performance management frameworks the place of an adequately designed rewards and penalties system is important (Kaplan and Norton, 1996; Otley, 2003). But in the case of HMCE, it was discovered that the accountability framework of the private sector can not work in entirety in the HMCE as the rewards and penalties system was not well developed in this organisation. Kaplan and Norton (2001) observe that making people accept a totally different way of measurement is hard if the change is not reinforced through incentive



compensation<sup>99</sup>. Under RAB, the new system of funding was provided to the HMCE by the Treasury, in terms of the policy targets of PSA. However the performance targets could not be allocated to the individuals in a cascading manner, as explained in chapter 10. Similarly, achieving the targets or not achieving them did not result in any rewards and penalties. Therefore it can be argued that in the case of HMCE, the PSA framework had a well defined planning role but it had rather a less developed control function.

### **11.3 Reciprocity in Accountability Relationship**

Johnsen (2001: 321) cautions against uncritical adoption and implementation of the BSC in public management as, he argues, this may result in reintroducing a Soviet-type, central planning model in political institutions. This is more likely, the author contends, if the underlying assumption is that of one principal and unambiguous goal for the organisation. The RAF developed in this PhD study (with the analysis of accounting changes in the period 1997-2003, and of discourse of HMCE interviewees and tax advisors) also cautions against such a one sided notion of organisational performance. It can be argued that the definition of accountability relationships depends on the definition of performance important to a stakeholder. If the tax administration defines the accountability relationships it would see them through the traditional ethos of

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<sup>99</sup> Kaplan and Norton (2001) argue that often PMS contain non-financial measures, which are used more like checklists of measures for managers to keep track of and improve than a comprehensive system of linked measurements. They distinguish multidimensional approach from the traditional approach by stating that all the measures flow out of the organisational strategy (Kaplan and Norton, 1996). One strong indication of considering all the important operational measures together can be found in the rewards system associated with achievement of targets.

law enforcement imprinted on its organisational mind (Stinchcombe, 1965: p 154). Therefore, it would define performance as collecting more revenue and reducing tax evasion. Consequently, 'customer-focus' will be viewed as a driver/determinant of the final result of revenue collection. However, if performance is viewed from the taxpayers' perspective then the performance and accountability framework has to be seen as comprising two sets of accountability relationships. The RAF is based on the central notion of '*reciprocity*' of accountability relationship which is argued to be more pronounced, in terms of formal accounts taking and giving, in the case of tax departments. It is this feature which distinguishes the accountability system of taxation organisations from other service delivery organisations in the private and public sectors.

The basic premise of the RAF is that the Board (i.e. the policy formulating body) of a tax administration and the tax payers are reciprocally accountable to each other. The taxpayers are accountable to the Board, through the operational level tax collectors, for their tax liabilities. The PMS for this kind of accountability or code of accountability (Gray and Jenkins, 1993) is based upon PIs such as revenue collection, fraud detection, and other enforcement activities. In a reversal of accountability relationships, the Board is also accountable, through the Government, to the taxpayers for the concerns of the taxpayers as citizens. These include respect for civil rights, reduction in compliance and psychic costs, making tax system simpler and provision of high quality services to the taxpayers so that they can pay taxes without any problem. This reciprocal relationship is shown by diagonal BD in Fig 11.1.



In the accountability system of a tax department the taxpayers, the tax collectors, the Board and the Government employ various influence strategies to see its *accountability* relationship become the most dominant one. The Government uses its resource dependence power (Pfeffer, 1992; Pfeffer and Salancik, 1978), reinforced by legal powers, to influence the tax department through managerial accountability. The tax payers can exercise influence by resorting to tax planning and avoidance strategies. The tax collectors can invoke their legal powers of law enforcement. The Board has managerial powers to keep the tax collectors in line with the official policy. The tax collectors have the power of professionalism and actual field knowledge, i.e., as agent they can take advantage of ‘information asymmetry’ (Brignall and Modell, 2000). In addition to these strategies both the tax payers and the department (the Board and tax collectors) also solicit the support of other actors who are indirectly connected with the system and can exercise *external accountability* powers. For instance the actors in RAF can approach judicial forums like Tax Tribunals and courts, if they have a grievance. The taxpayers also use public opinion making bodies like media, trade bodies, and political parties to keep a check upon tax collectors’ powers. The legislature (through select committees) acts on behalf of both taxpayers and tax collectors by reviewing the tax system regularly and by giving audience to the representatives of both taxpayers and tax collectors.

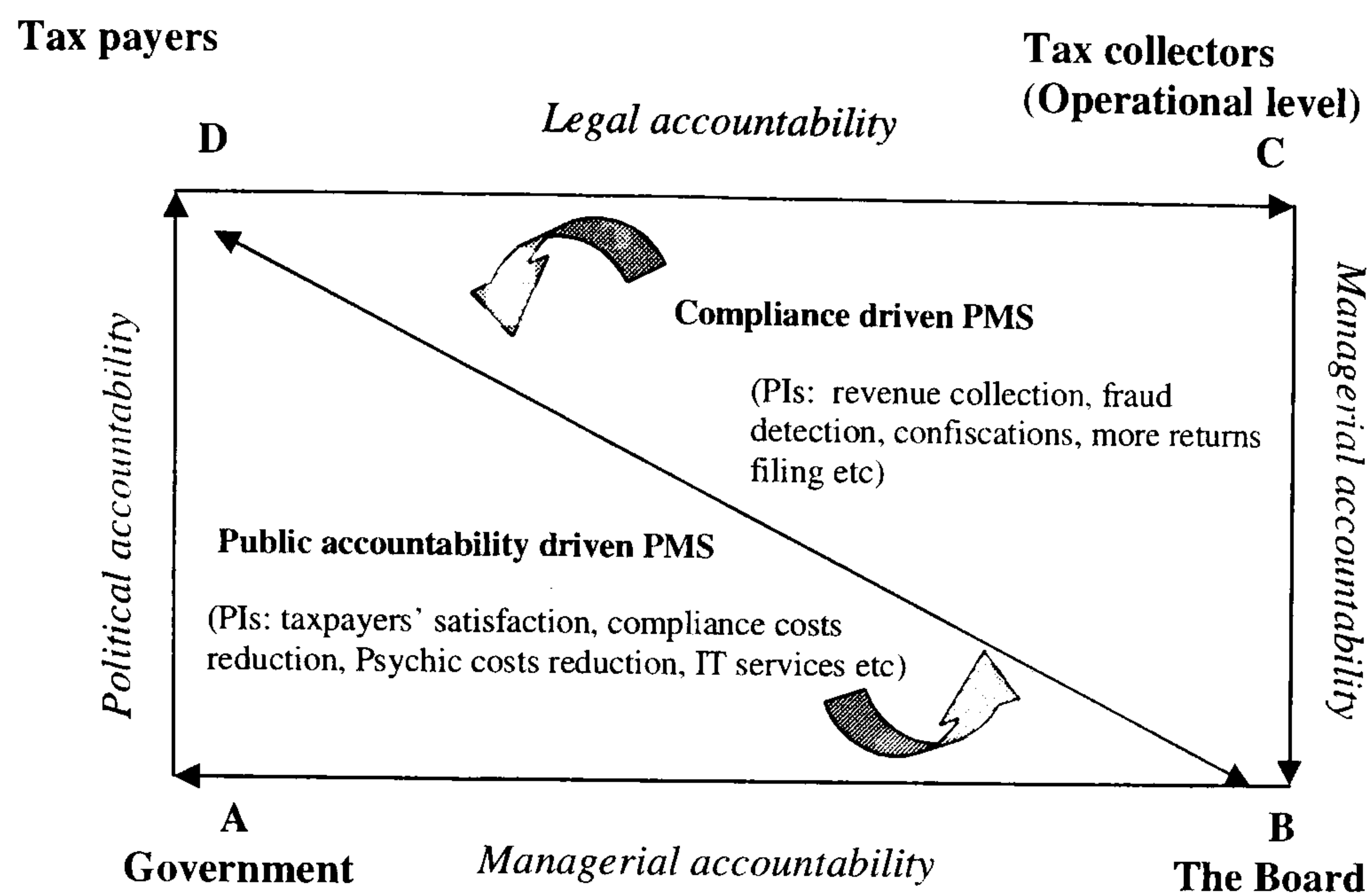


Fig 11.1 Dilemma for tax administration

There is an important consequence of the RAF for PMS of a tax administration. There is a need for striking a fair deal between the demands of both taxpayers and tax administration. If left to the taxpayers, they would like to see the whole rectangle occupied by their concerns. Similarly, if left to the tax administration, it would like to see only revenue collection related PMS occupying the whole rectangle. In wake of this likely competition, the ideal policy framework is one where the concerns of both tax administration and taxpayers are accommodated in equal importance. When an organisation does not achieve symmetry in terms of RAF, it is either compliance driven or public accounting driven. In the former, the PMS favours the concerns of resource provider for more tax revenue, while in the latter the concerns of taxpayers gain greater importance.



Two qualifications are important for making a RAF symmetrical. First, the PMS of the tax administration should contain measures which provide information to both the taxpayers and the Government (the resource provider) so that, as a principal, they can assess the performance of the tax administration, as an agent. Secondly, and more importantly, the measures/PIs relating to the two competing perspectives of performance should be treated as equally important. Kaplan and Norton (2001) argue that mere inclusion of a few non-financial measures which are used as a checklist does not make a PMS multi-dimensional. What is more important is how the non-traditional measures of performance are actually used for reporting performance. A PMS can become symmetrical if performance on both perspectives is not only measured but, more importantly, is also reported and highlighted in the textual reports of organisational performance. In the case of HMCE it was found that the poor performance on the dimensions of taxpayers' satisfaction and productivity according to PSA 2000 were not mentioned in the textual reports at all. Such a PMS can be termed as multi-dimensional in appearance but not in spirit..

#### **11.4 The PMS of HMCE**

The PhD case study was carried out in order to answer the following research question.

*“How are accountability relationships defined and operationalised with the help of performance measurement in the case of a tax administration and to what degree NPM inspired accounting changes alter such relationships?”*

The ‘middle range thinking’ advised by Laughlin (1995) was adopted in order to design the case study. The skeleton of NPM framework of accounting changes in the case of a tax administration was fleshed with empirical evidence gathered

from triangulated sources of primary and secondary textual data. The analysis helped in development of RAF in chapter 8 which was revisited in the earlier section. The RAF answers how are accountability relationships defined and operationalised with the help of performance measurement in the case of a tax administration. Using the same framework, the second part of the research question is answered in Fig 11.2.

In chapter 6, reference was made to the PMS practices in OECD countries (OECD, 2001). The PIs were found to be categorised as ‘productivity’, ‘quality’ and ‘effectiveness’. Already, a warning had been raised that such terms do not have standard / uniform definitions. However, if PMS of HMCE is reviewed with regards to the definitions provided by OECD report, it can be stated that ‘productivity’ has been a measure of performance which remained a part in all PMS despite many rounds of accounting changes. This is because the Treasury has prescribed it as a fundamental measure of performance for all Government departments. However, defining ‘productivity’ has remained a source of problem for HMCE, especially when outputs were defined in terms of customer-focus in PSA 2000.

The second category, *Quality* was made a part of PSA 2000 framework, as increasing taxpayers’ satisfaction became a part of the high level targets. In PSA 2002, though references are made to improving services provided to the taxpayers, there are no specific targets for this dimension of performance.



The third category, i.e. effectiveness, was not present in the PMS frameworks of HMCE. However, with adoption of tax gap approach, ‘effectiveness’ (measured by tax gap reduction) has become the defining feature of PMS introduced by PSA 2002.

In chapter 5 a three point categorisation was proposed to classify PMSs of tax authorities. The PMSs of HMCE during the period of analysis 1997-2003 can be summarised as moving on this categorisation line in the following fig:

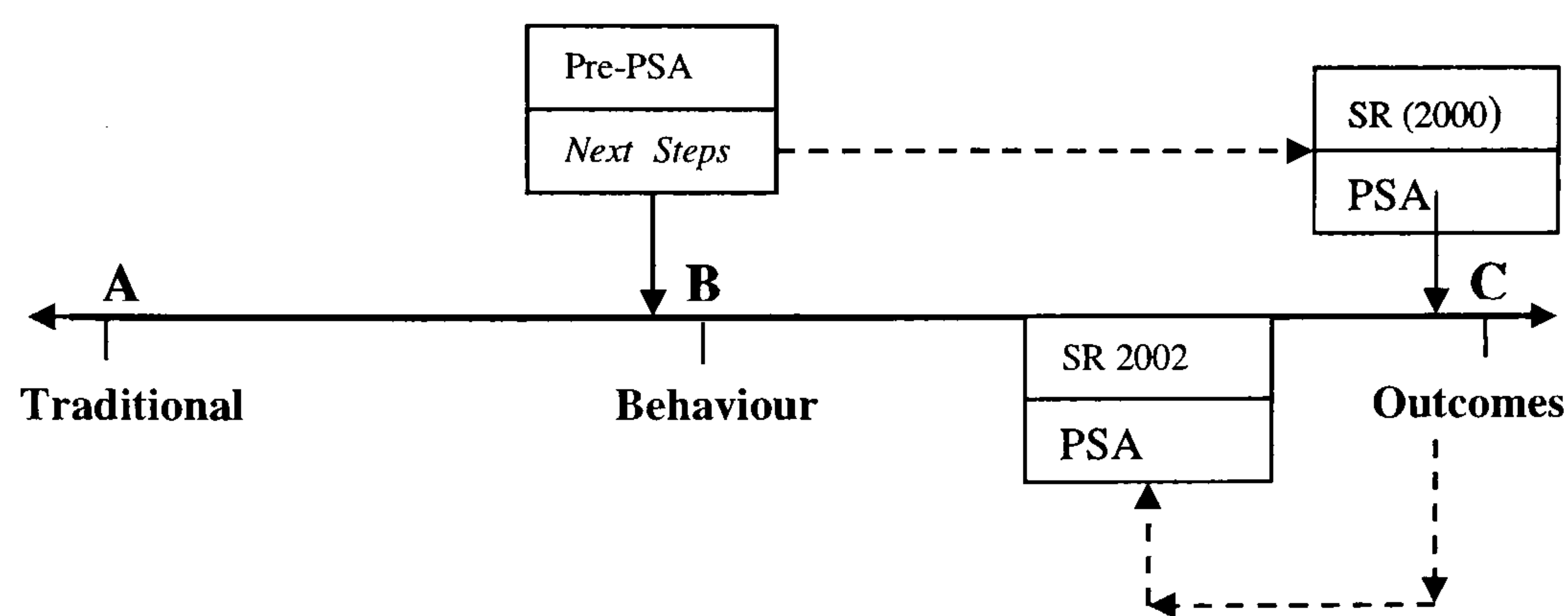


Fig 11.2: Movement of PMS of HMCE during 1997-2003 period

As can be seen the PMS of HMCE before 1998 is positioned near point B where performance was measured and reported by mainly revenue collection related PIs and partly by customer-focused PIs. It was, therefore, public accountability driven PMS. With PSA (2000), the performance measurement moved to multidimensional outcomes as both compliance and customer-focus outcomes were measured in equal importance. This created tension like situation for the management, as explained in chapter 8. Arguably, as a coping strategy, HMCE adopted the ‘tax gap’ based PMS in PSA 2002. In this approach though outcome measurement is used but a noticeable point is that a single measure of ‘tax gap’

minimisation attains greatest importance. The PIs used for reporting 'tax gap' reduction are the traditional output measures like revenue increase and anti-evasion. In view of this it can be argued that the PSA 2002 resorted to the traditional PMS but under the guise of tax gap outcome measurement. No doubt, the PSA 2002 contains a few measures related to customer-focus as well. But those are of secondary importance, and appear as the determinants of tax gap reduction (Fitzgerald et al., 1991). Since the PSA 2002 has the features of both multi dimensional outcome measures and traditional measures of performance, it is positioned between points B and C on the categorisation line in Fig 11.2

The PhD evidence establishes that within the department performance is still defined in terms of revenue collection figures even though there has been a conscious effort to distance itself from this traditional notion of performance and move towards a more multi-dimensional performance framework. '*What is measured, gets done*' appears to be the conventional wisdom in the literature. But 'what is done, gets measured' explains more aptly the PMS of HMCE. This can be argued that the tax gap based PMS is a more refined version of greater revenue collection, as the tax gap is minimized if more revenue is collected as compared to the previous years. Since targets are not handed down to the individual level, performance measurement has a limited role in performance management. At the top level, performance data is used for planning and feed-forward control purpose but the feedback control mechanism is not developed for lack of a fully operational reward/penalty system.



### **11.5 Notion of Accountability**

The NPM literature assumes a causal relationship between performance measurement, accountability and performance improvement (Cunningham and Harris, 2001: p 146). Day and Klein (1987) in their study on accountability in five public sector organisations (Social Services Committee, Education Committee, Police, NHS and Water Authority) term their experience of interviewing the members of these organisations as a “visit to a strange tribe, whose existence is taken for granted in the theoretical literature on accountability” (p 72). The authors therefore lament the fact that views of members of organisations remain largely unexplored even though they have crucial importance. How is accountability conceptualised in the case of a tax administration like HMCE? The need for understanding accountability in the case of HMCE becomes even more important when even a Government publication acknowledges the fact that:

“Although many organisations understand the theory behind improving accountability for results, it doesn’t always translate into practice and implementation is often fudged” (HM Treasury, 2002b: p 3).

The Treasury *Chief Secretary* in his foreword of the publication also underscores the need for clarifying accountability relationships at all levels in an organisation for better performance.

The interviews with the managers and other tax officials of HMCE established that accountability was mostly conceived as managerial or legal. The notion of public/political accountability or customer-focused accountability was not found to be a part of the official discourse. It is basic theme of this PhD thesis that PMS

operationalises accountability relationships. However, it is not clear from PSA frameworks which accountability relationships had been strengthened? For instance, how would we know if all forms of accountabilities have been improved and hence the organisational performance? What if compliance targets are met, but customer satisfaction target or compliance costs reduction target are not met? Do these measures and targets enjoy same importance, or is it that the traditional targets have a sway over the non-traditional ones? In chapter 6, while analysing the OPA (i.e. PSA, 1998) of HMCE, it found that the senior managers of governmental organisations were reluctant to see their organisational performance audited by an external auditor such as NAO. Since the NAO reports still do not comment upon PSA targets and organisational performance, it can be argued that formal systems of accountability are still not very robust in the case of HMCE. Moreover, the discursive importance given to traditional performance measures in the Annual Reports suggests that they still govern the notion of performance in HMCE. Therefore it can be concluded that accountability is still a muddled notion in the case of HMCE, where traditional forms of legal and managerial accountabilities reign supreme.

Theorising the interaction of various accountability relationships in a situation where the principal and agent can have reciprocal roles is not well addressed in the literature. Through this PhD research, a framework for analysing accountability relationships by ‘accounts giving and taking’ in a situation of reciprocity was developed. This way it fills an obvious gap in the accountability related literature.



## 11.6 Role of Accounting Changes

The PhD research was based on the premise that if the accounting changes were successful, the discourse of the interviewed line managers and operational level employees would reflect the intended changes of customer-focused accountability and service delivery. However little evidence of this nature was found in the discourse of the employees<sup>100</sup>.

In chapter 2 three camps of authors were identified with varying degree of stress upon the effectiveness of accounting as a change management tool. First, the normative writers (e.g. Kaplan and Norton, 2001; Likierman, 2000, 1993) advocate a primary role for accounting in effecting organisational changes<sup>101</sup>.

Proposing BSC in 1992, Kaplan and Norton claim that:

“... Originally, we thought the Balanced Scorecard was about performance measurement ... Once organizations developed their basic system for measuring strategy, however, we quickly learned that measurement has consequences far beyond reporting on the past... Thus the Balanced Scorecard concept evolved from a performance measurement system to become the organizing framework, the operating system, for a new strategic management system” (Kaplan and Norton, 2001: p 99).

The opposing view sees accounting as a mere legitimating tool in the hands of change managers, for instance Cooper (1980, p. 164) claims that:

“accounting may be viewed as a means of sustaining and legitimizing the current social, economic and political arrangements”

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<sup>100</sup> This is not to suggest that the interviewees were inattentive to the need of better behaviour towards the taxpayers. In fact they seemed to view “positive success” i.e. achieving good results with a good behaviour important. But the managerial emphasis on treating taxpayers well was found unrelated to the PSA measures as there is little evidence of *ownership* of PSA related measures among managers and employees. Hence no evidence was found which could suggest any fundamental change in the organisational ethos of HMCE caused by changes in the performance measurement framework of the HMCE.

<sup>101</sup> Kaplan and Norton (2001, 1996) warn that mere awareness of corporate goals is not enough to change people's behaviour. They stress that the organisation's high-level strategic objectives and measures must be translated into objectives and measures for operating units and individuals in order to have a strategic shift.

Richardson (1987) reviews the views of this sceptic class of writers and concludes that the common focus of these papers is the ability of accounting, as a set of beliefs and techniques, to link actions and values, i.e. to make those actions legitimate.

The two views on the role of accounting can be seen as a question as whether accounting has the ability to take on the role of a choreographer or is it that it merely participates as a dancer in ritualistic dancing of reforms?

Located in the middle of the two extremes, *rationalists* adopt a *processual* approach and consider the context of an organisation important without professing any ideological loyalty.

The evidence in the case of HMCE establishes that the attempts of NPM inspired reformers to change the ethos of the HMCE with the help of accounting changes did not succeed. Otley (2003) also argues that without changing the cultural norms of an organisation there is little likelihood of success for accounting changes. It was found in this PhD study that not only the traditional revenue figures based PMS' regained its dominance in the PSA framework but the perception of the clients of the HMCE also did not change after customer-focused PMS (i.e. PSA 2000) was implemented. This is best explained by the following remarks of one of the VAT practitioners:

“Customs say they are trying to be customer-focused and helpful, have undoubtedly put efforts into doing this, backed by well intentioned people, but so far have only proven the saying that a leopard cannot change its spots” (VP2: emphasis added)



According to OECD (2001:4) revenue and additional revenue recovered by audits can be regarded as both 'output' or 'outcome' of the activities of the tax officials. It can, therefore, be contended that HMCE continued to use 'revenue' and 'extra revenue' as measures of performance; though under the guise of 'tax gap' reduction outcome. It can also be argued that the whole process aimed to gain 'legitimacy' in the wake of coercive pressures generated by the NPM inspired reformers in the central government (Kurunmaki et al., 2003). In terms of Laughlin (1991)'s framework of organisational changes the PSA frameworks can be termed as a first order change which had an effect upon the *design archetype* but the *interpretive schemes* did not alter at all. Therefore, it can be argued that the accounting changes were internalised through the policy of *reorientation* (ibid) or *manipulation* (Oliver, 1991).

Doig and Graham (1998) and Colville et al (1993) discuss dancing of HMCE to the governmental tunes of the then Conservative government. Interestingly, the dancing has continued under different tunes and labels ever since. The PhD research therefore found that quick fix solutions that ignore the context of an organization end up becoming a ritual dancing, where accounting jumps in to perform its part of the ritual. While the important role of accounting in accountability systems and change management is not dismissed, the evidence of this case study does not support the hypothesis that accounting can always play an effective role as a choreographer. Both past and present instances of organizational reforms in HMCE suggest that reforms, accounting changes

inclusive, have little chances of success if the core functions do not inform the intended changes<sup>102</sup>.

Despite the preceding findings, however, like Oliver (1991), this PhD researcher also does not believe that responding to the normative or coercive pressures is always for the sake of legitimacy and thus not rational. It is possible that changes introduced in response to the normative pressures are not self motivated but reflect a rational decision ensuring real dividends in the future. But what is of essence here is the importance of context of an organisation. Roberts and Scapens (1985: 443) also stress the same point as they argue that understanding accounting practices in their organisational contexts requires more than a technical description of accounting information systems as they are conceived and designed in abstract. Even in the private sector many organisations have realised that following generic causal models does not necessarily ensure success. For instance, Ittner and Larcker (2003:93) and Pawson (2002: 179) argue that businesses often make the mistake of using performance measures without giving careful attention to their own contextual factors.

The PhD research shows that off-the-shelf accounting reform device had difficulty of operation in the specific context of a tax administration like HMCE. This substantiates Otley's (2003) observation that control systems are built on a foundation of shared values and assumptions. The PhD research found that the

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<sup>102</sup> Somewhat similar conclusion was drawn by Ball (2001) who after reviewing the benchmarking initiatives in the Local Government management concluded that *benchmarking* had skilfully been subsumed into established patterns aligned with 'new' management thinking. It is argued that the vast benchmarking related data was hardly used for managerial purpose.



culture of HMCE was not given consideration while the NPM inspired PSA framework was implemented.

It was found in section 9.5 earlier that in the O'Donnell report which recommended the merger of HMCE with IR, a full chapter is devoted to the issue of accountability besides explaining efficiency savings and customer focus. It is claimed that by separating policy (*the Treasury to be responsible*) from implementation (*the HMRC to be responsible*) the accountability framework would be improved. Interestingly same set of reasons were cited in the official publications for introducing PSA and SDA framework (HM Treasury, 2000d; p 3). The repetition of the same policy ideals, therefore, further substantiates the finding that the earlier accounting changes based initiatives failed to deliver. This also signifies the fact that successful organisational changes require greater effort, as deep organisation changes can only be successful if the context of an organisation is understood and a good case for change is made so that the change effort is owned by all across the organisation (Burke, 2003).

## **11.7 Contribution of the PhD Research**

This PhD study makes contribution to the corpus of knowledge in three main ways.

### **11.7.1 First Study of PMS of a Tax Administration**

Boden et al. (1998: 268) argue in their paper on NPM's implementation that despite very functionalist rationality of NPM when the standardized NPM techniques are implemented in organisations where typical service delivery

processes do not exist the results can become “idiosyncratically problematic”. The case study of HMCE is therefore important that this organisation is not like a typical service delivery organisations such as hospitals, schools or passport agency. It is even different from other law enforcement outfits like the police and the armed forces as the services provided by these organisations are comparatively easier to define. In the case of a tax administration like HMCE a great deal of conceptualisation is required in order to define the building block notions of NPM such as customers, customer focus and service delivery. The fact that no research on accountability and PMS in tax authorities had been done so far was, therefore, an important gap in the literature.

Lapsley (2000: 172; 1999: 206) stresses the need for researching management accounting innovations in the various contexts of the public sector organisations. He argues that research in various types of public sector organisations is essential so that the question of using management accounting as a strategic tool in the public sector is answered more conclusively. This PhD study is the first ever research which considers the impact of NPM inspired accounting changes in the context of a tax administration. It, therefore, has addressed the calls made by management accounting scholars like Lapsley, Hopwood, Broadbent and Guthrie for research in different and new types of organisations, and therefore fills the obvious gap in literature. The research also addresses the calls made by Tomkins et al (2001) for more research on tax management issues. In this way the research opens up the tax management as a potentially interesting and important research site for other researchers.



### **11.7.2 Notion of *Reciprocity* in Accountability Relationships**

While many studies have addressed the accountability systems underscoring various types of complexities, the notion of *reciprocity* and its operationalisation has not received much attention. The PhD study has developed the notion by analysing the performance measures of HMCE during the 1997-2003 period and by categorising them on the basis of reciprocity of accountability relationships. The PhD research, therefore, enriches the literature on accountability systems by developing the notion of *reciprocity* in the ‘principal-agent model’ of accountability which then led to the development of RAF for tax authorities. The framework not only emphasises reciprocity in accountability relationships but also lays emphasis on modification in accountability relations with the help of changes in PMS. The emphasis of performance measurement literature has been on using performance measurement for enhancing the accountability relations. The PhD study makes a contribution by considering the use of performance measurement for modifying the accountability relationships when the two actors (i.e. the taxpayers and the tax collectors) are principal and agent to each other in their reciprocal roles. The social structure of a tax administration, in terms of Giddens’ structuration theory (Giddens, 1984), can be best understood by referring to the performance measurement practices over a period of time. The RAF developed in this PhD can become a very helpful tool for such kind of analysis.

### **11.7.3 Role of Accounting Changes**

In this PhD research, the pathways of changes during 1997-2003 were tracked and it was found that the accounting changes failed to achieve the NPM inspired

customer-focus in the case of HMCE. While this research was in process, interestingly, Cavalluzzo and Ittner (2004) carried out a study of similar nature in public sector organisations in the U.S. They also found little evidence that the perceived benefits from the mandated performance measurement initiatives in the US government increase with greater measurement and accountability. Referring to institutional theories, they also conclude that systems implemented to satisfy external requirements are less likely to influence internal behaviour than are those implemented to satisfy the organization's own needs. This in-depth PhD study of HMCE furnishes evidence of same nature in the case of a big central government organisation in the U.K.

Burns (2000: 568) calls for more case studies which explore the temporal dimensions of change, unfolding over time, through reference to the past, the present and the future. Clark, et al. (1988, p. 222) also stress the need for such a 'processual' approach to accounting case studies:

"Apart from its analytical and explanatory value in particular cases, the processual approach also sensitizes us to the fact that there are no fixed outcomes of change under a given system, simply outcomes at particular moments in time".

The PhD study was based on this 'processual' approach and, therefore, enriches our understanding of how accounting changes create difficulties in terms of defining performance and how organisations respond to such difficulties through various coping mechanisms.



### **11.8 Future Research**

The PhD research made inroads into an unexplored research site of tax management. The prospects for future research in this site are enormous. In the PhD thesis a generic framework for classifying PMSs of tax authorities of both developed and developing countries was proposed. Future research can carry out empirical investigation to find how many tax authorities fall in the categories proposed by this PhD research. Additionally what are the determinants for a tax authority to fall under a particular category can also be an interesting research question. An accountability framework (RAF) was developed in the PhD research to examine the PMS and accountability relations in the case of a tax authority. In future surveys can find out what are the determinants for a tax authority to adopt a compliance driven or public accountability driven framework of PMS.

Further research can also be carried out on various managerial issues of tax authorities. For instance, it was found in this PhD research that the PSA changes in respect of HMCE could not deliver the desired results, therefore, it would be interesting to investigate the extent of success of merger on the criteria of efficiency savings, customer focus and accountability in 3-5 years time. The PhD research has provided a holistic view of performance in the context of a tax administration. Future research may also now look into narrower areas of performance such as debt management, productivity, tackling VAT frauds etc. The list is virtually endless, and therefore, the area of tax management can be rewarding for any interested researcher.

**Annex 2.1 List of Accounting Journals Included in the Empirical Analysis**

<b>No</b>	<b>Journal</b>	<b>Private</b>	<b>Public</b>	<b>Total</b>
1	Management Accounting Research	29	7	36
2	Accounting, Organisations and Society	15	1	16
3	Journal of Accounting and Economics	9	0	9
4	Journal of Accounting Research	7	0	7
5	The Accounting Review	6	0	6
6	Journal of Management Accounting Research	5	1	6
7	British Accounting Review	5	0	5
8	European Accounting Review	3	2	5
9	Journal of Accounting and Public Policy	4	1	5
10	Accounting Horizons	4	0	4
11	Accounting Forum	3	0	3
12	Critical Perspectives on Accounting	1	1	2
13	Journal of Accounting, Auditing & Finance	2	0	2
14	Management Accounting Quarterly	1	1	2
15	Accounting, Auditing & Accountability Journal	1	0	1
16	Contemporary Accounting Research	1	0	1
17	Journal of International Accounting, Auditing and Taxation	1	0	1
18	Journal of International Financial Management and Accounting	1	0	1
19	Abacus	0	0	0
20	Accounting and Finance	0	0	0
21	Accounting & the Public Interest	0	0	0
22	Behavioural Research in Accounting	0	0	0
23	The International Journal of Accounting	0	0	0
24	Journal of Accounting Literature	0	0	0
25	Journal of Business Finance & Accounting	0	0	0
	Total	98	14	112

Public = Articles on public sector related PMS

Private = Articles on private sector related PMS



**A. Personal Introduction**

1. When did you join Customs and Excise? What career postings you have worked at?
2. How would you describe the work which you do?
3. What type of training programmes did you undergo at the time of joining the service or thereafter?

**B. Audit Work**

4. How is the audit work assigned to you? Who selects and in what way, the businesses you audit?
5. In what ways your work is similar to the work of other assurance officers and to what extent it is different?
6. In the wake of recent reforms and changes in the organization, how and to what extent your work has been affected?
7. How do the businesses react/interact when you visit them?
8. What are the most problematic areas relating to your work?

**C. PMS Issues**

9. Have you received any instructions in connection with PSA or SDA?
10. How do you report your performance? What measures/indicators are used to record and report your performance?
11. Do you see any significant changes taking place in use of performance measures and reporting compared with say five years back?
12. In what way this performance data is used by the office and the organization as a whole?
13. Are you given any **specific targets** in connection with VAT like revenue to be collected, or assurance revenue? If yes, how do you manage meeting those targets?
14. How would you describe your **appraisal system**? First lets talk about over all appraisal of the office; how is reporting done? Second, at individual level, how is appraisal carried out? Is performance of managers and employees working in HMCE formally appraised or is it an informal affair?
15. What **criteria** are important to you when you **appraise** your staff members?
16. What **criteria** do you think is followed when your work is assessed by **superiors**?
17. Are there any **significant changes** which you might have noticed during last, say five years, as far as **performance appraisal** is concerned?
18. How do you differentiate a good performer from a bad performer?
19. What is the system of rewards and penalties in terms of performance appraisals?
20. How is the PA related to promotion, bonus pays, and postings?

**D. Customer focus**

21. In the official discourse taxpayers are often termed as customers? How can taxpayers be called customers? What are your views?
22. How has this renewed emphasis affected your and your teams' work? Do you measure performance of your staff on that account?
23. Some critics say that in private sector, the most vocal customers usually are most served. Isn't it that similar attitude would lead to inequalities among customers of public sector?
24. Some tax practitioners are of the view that VAT people treat all businesses as criminals and use highhanded tactics as compared to Inland Revenue? How far that impression is justified?
25. If you have targets of assurance related recoveries and *nice guys image*, which target is going to matter most to you? Do you subscribe to the view that the targets compete with

each other and the staff behaviour is influenced more by traditional performance indicators like revenue and cases figures rather than new measures which do not relate directly to your professional work?

26. How can the perception of VAT staff be improved among small businesses? Do you think that target indicators measuring customer satisfaction can help improve the situation?

#### **D. Diversity and equality**

27. Are **diversity** and **equality** demands kept in view when appraisals are done? In what way and to what extent?
28. What is the impact upon overall performance measures when allowances are made for diversity and equality?
29. Do you believe that there exists reciprocity of accountability between tax managers and tax collectors?

#### **E. Accountability**

30. How is accountability viewed and perceived in your organisation? How can accountability be **operationalised** in a public sector organization especially in a tax department?
31. What are different **types of accountability** pressures that you as a tax manager experience?



**Primary Sources of Textual Data**

Category	SNo	Document Title or code	Reference
<b>Interviews</b>			
	1	SM1	Senior Manager VAT Operations
	2	SM2	Senior Manager VAT Operations
	3	MM1	Middle level Manager
	4	MM2	Middle level Manager
	5	MM3	Middle level Manager
	6	MM4	Middle level Manager
	7	MM5	Middle level Manager
	8	MM6	Middle level Manager
	9	MM7	Middle level Manager
	10	HQ1	HQ level Manager
	11	HQ2	HQ level Manager
	12	HQ2	HQ level Manager
	13	HQ3	HQ level Manager
	14	HQ4	HQ level Manager
	15	OL1	Operational Level Assurance Officer
	16	OL2	Operational Level Assurance Officer
	17	OL3	Operational Level Assurance Officer
	18	OL4	Operational Level Assurance Officer
	19	OL5	Operational Level Assurance Officer
	20	OL5	Operational Level Assurance Officer
	21	JH	Dr John Hasseldine, Nottingham University Business School, U.K
	22	RB1	Dr Rebecca Boden, Bristol Business School
	23	RB2	Dr Roger Bowles, University of York
	24	ZK	Secretary, Commonwealth Tax Institute, London
	25	RK	Secretary, VAT Advisors Group.
<b>Written replies</b>			
	1	RKL	Secretary, VAT Advisors Group.
	2	MCL	HQ level Manager
	3	VOL	VAT Operations reply
	4	SML	HQ level Manager
	5	VA1 to VA20	VAT Advisors
<b>Documents obtained</b>			
	1	BNS	Business Needs Survey Questionnaire
	2	VS	VAT strategy
	3	OS	Organizational charts for RBS
	4	PR	Local Performance Reports

- 1 Cm 6163, *Financing Britain's Future: Review of the Revenue Departments* by Gus O'Donnell Presented to Parliament by the Chancellor of the Exchequer by command of Her Majesty, March, 2004, London, HM Treasury
- 2 Cm5922, Treasury Departmental Report, 2003, HM Treasury  
[http://www.hm-treasury.gov.uk/media/F74/94/Deptrep03\\_Chapt2\\_64kb.pdf](http://www.hm-treasury.gov.uk/media/F74/94/Deptrep03_Chapt2_64kb.pdf) (seen 3-12-03)
- 3 *Civil Service Statistics, 2001*, London, Cabinet Office, 2002  
[www.civilservice.gov.uk/statistics](http://www.civilservice.gov.uk/statistics) (seen 3-12-03)
- 4 *Managing Resources: Accountability*, London, HM Treasury, 2002
- 5 The second phase of public sector reform: The move to delivery. Cabinet Office, 2002  
[Http://www.cabinet-office.gov.uk/eeg/secondphase.htm](http://www.cabinet-office.gov.uk/eeg/secondphase.htm), (seen 3-12-03)
- 6 *Reconciliation of SR2000 PSA targets with SR2002 targets*, HM Treasury, 2002  
[www.hm-treasury.gov.uk/media/1DDCD/PSA%20reconciliation.pdf](http://www.hm-treasury.gov.uk/media/1DDCD/PSA%20reconciliation.pdf)
- 7 *Analysing resource accounts: user's guide*. June, London. HM Treasury, 2001
- 8 *Choosing the Right FABRIC: A Framework for Performance Information*. London. HM Treasury, 2001 [http://194.200.85.88/performance\\_info/fabric.pdf](http://194.200.85.88/performance_info/fabric.pdf) (seen 3-12-03)
- 9 Cm 4915, *Service Delivery Agreements 2001–2004: A Guide*, London, HM Treasury, 2000  
<http://archive.treasury.gov.uk/sr2000/sda/whitepaper/guide.pdf> (seen 3-12-03)
- 10 Cm 4807, *Prudent for a Purpose: Building Opportunity and Security for All: 2000 Spending Review: New Public Spending Plans 2001-2004*, HM Treasury, 2000
- 11 Cm 4310, *Modernising Government*. London: Cabinet Office, 1999  
[Http://www.cabinet-office.gov.uk/moderngov/download/modgov.pdf](http://www.cabinet-office.gov.uk/moderngov/download/modgov.pdf) (seen 3-12-03)
- 12 *The Government's Measures of Success: Output and Performance Analyses*, London HM Treasury, 1999 <http://archive.treasury.gov.uk/pdf/1999/opa.pdf>. (seen 3-12-03)
- 13 Cm 4181, *Public Services for the Future: Modernisation, Reform, Accountability. Comprehensive Spending Review: Public Service Agreement 1999–2002.*, HM Treasury, 1998 December
- 14 Cm 4011, *Modern Public Services for Britain: Investing in Reform*, July, HM Treasury, 1998  
<http://www.archive.official-documents.co.uk/document/cm40/4011/4011.htm> (seen 3-12-03)
- 15 Cm 2929, *Better Accounting for the Taxpayer's Money: The Government's proposals; resource accounting and budgeting in government*, HM Treasury, 1995
- 16 Cm 2626, *Better Accounting for the Taxpayer's Money: resource accounting and budgeting in government*, HM Treasury, (1994)



Annex 3.4    **Important Strategic Level Publications of HMCE**

SNo	Document Name	Publication date	Importance
1	Protecting indirect tax revenues (PITR)	November 2002	The fundamental strategy paper spelling out tax gap based strategic approach.
2	Tackling Indirect Tax Fraud	November 2001	The forerunner of PITR which laid the basis of the new approach.
3	Tackling Tobacco Smuggling (TTS)	March 2000	The paper introduced strategic outcomes based approach.
4	Measuring indirect tax losses (MITL)	November 2002	The paper spells put how the new approach will be measured.
5	Measuring Indirect Tax Fraud	November 2001	The forerunner of MITL
6	VAT Strategy	March 2002	The TTS based approach applied to VAT.
7	Public Service Agreement	1998, 2000, 2002	The high level document linking together strategy and measurement papers on one hand and aligning the HMCE approach with the overall Government approach on the other.

Annex 4.1

**Taxes Administered by HMCE**

The indirect taxes currently administered by HMCE are:

- VAT
- Excise duties, e.g. fuel, betting and gaming, cider, wines and spirits
- Landfill Tax
- Customs Duties on goods from outside the European Union.
- Climate Change Levy
- Air Passenger Duty
- Insurance Premium Tax
- Aggregates Levy

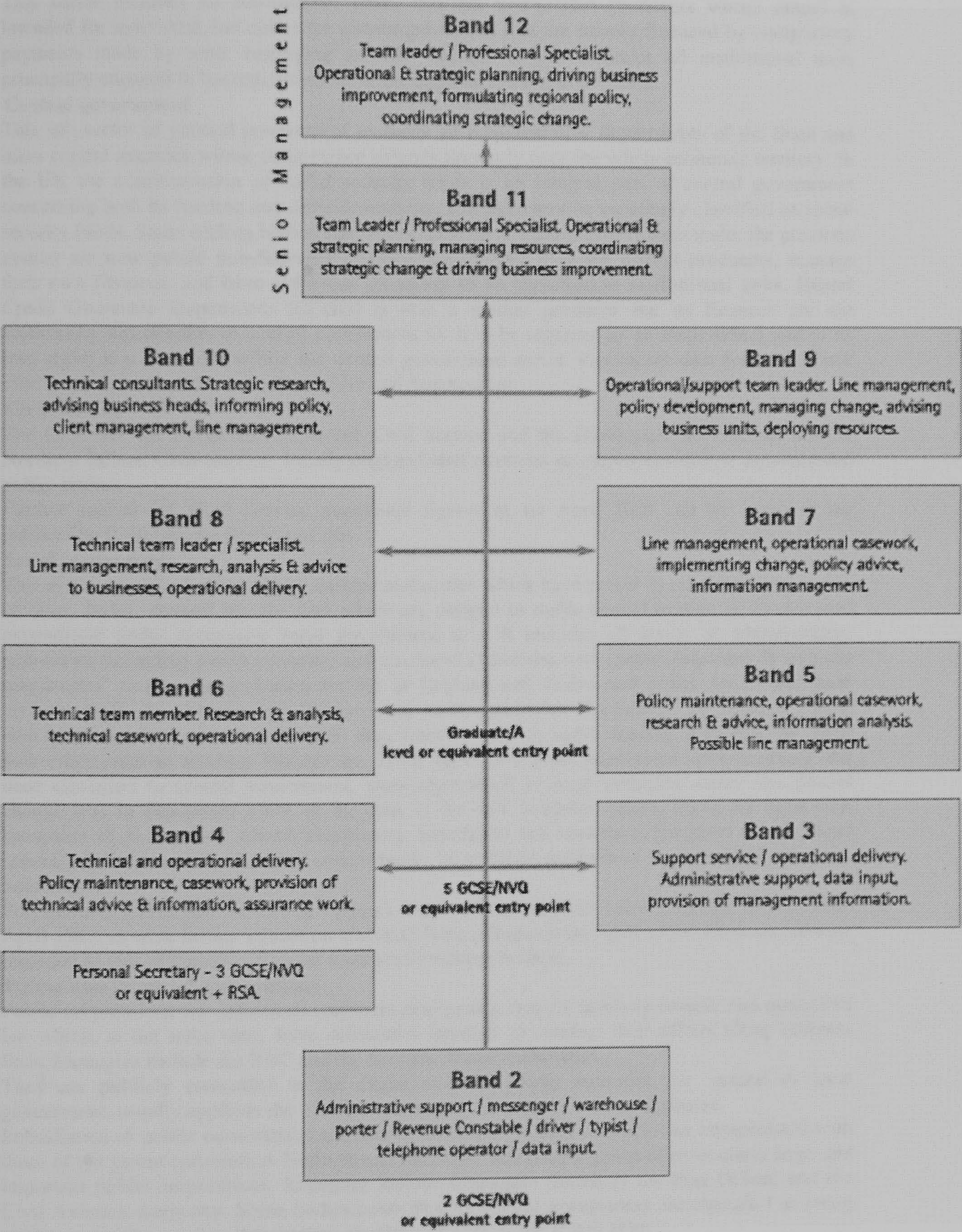
While customs, excise duties and VAT have been the major revenue spinners for the department, HMCE had been dealing with many other forms of duty/taxes which are now repealed. For instance, duties imposed on medicine were taken over from the Board of Inland Revenue in 1909 but were later abolished in 1941 under the Pharmacy and Medicine Act. Some other such examples have been tabulated as follows:

SNo	Name of levy	Year abolished
1	Railway passengers duty and unsuccessful betting duty	1929
2	Excise License Duties for appraisers, auctioneers, house agents and plate dealers	1949
3	Entertainment duty	1960
4	Playing card duty	1960
5	Television excise duties	1963
6	Television advertisement duty	1964
7	Retail liquor excise licenses	1967
8	Purchase Tax	1973
9	Passenger returns for the Department of Trade and Industry	1988
10	Match and mechanical lighter duties	1993
11	The Ships' Registry	1994 (transferred to Department of Transport)

(Tabulated from NDAD, 2003)



Levels of Personnel in HMCE





### Annex 4.3 The Sectors Falling Under the Definition of ‘Public Sector’

#### **General Government**

This sector includes all institutional units, that are non-market producers whose output is intended for individual and collective consumption, and that are mainly financed by compulsory payments made by units belonging to other sectors. It also includes all institutional units principally engaged in the redistribution of the national income and wealth.

#### **Central government**

This sub-sector of general government includes all administrative departments of the State and other central agencies whose competence extends normally over the whole economic territory. In the UK the administration of social security funds is an integral part of central government concerning both its funding and decision-making, and so cannot be separately classified as social security funds. Some trading bodies that were classified as central government under the previous system are now public non-financial corporations because they are market producers, manage their own finances, and have sufficient autonomy to be classified as institutional units. Export Credit Guarantee Department (ECGD) is also a market producer but its finances are not sufficiently independent of central government for it to be regarded as an institutional unit in its own right; it is therefore within the central government sector. Consistent data for years since 1961 appears in the Economic Trends Annual Supplement.

#### **Civil Service**

The Civil Service comprises the Home Civil Service and the Diplomatic Service but not the Northern Ireland Civil Service, locally engaged staff overseas or employees of non departmental public bodies.

Further analysis of Civil Service manpower figures at 1st April 2001 can be found in the publication Civil Service Statistics 2001.

#### **Local government**

This sector consist of all local government authorities which have power to raise funds by means of rates, levies, council tax etc. and which are obliged to make annual returns of income and expenditure under successive local government acts. It includes all levels of administrative authorities (including parish councils) and also local authorities with special functions. It includes magistrates' courts, the probation service in England and Wales and police forces and their civilian staffs. It embraces all functions of such authorities (including, for example, their education services and construction departments) and includes trading activities of local authorities, such as housing, theatres etc. From April 1999 grant maintained schools, which had been classified to central government, were reclassified to local authority status (the formal change was in September 1999, at the start of the new academic year). There are three new categories of mainstream school: community, foundation and voluntary. For grant – maintained schools, this means that, like other state schools, they will be maintained by their local education authorities.

Polytechnics and higher education colleges were transferred from local authority control from April 1989, as were further education and sixth form colleges from April 1993. These are all now regarded as part of the private sector (non-profit making bodies).

#### **Public non-financial corporations**

Public corporations are defined as corporate enterprises, that are publicly owned, and controlled but which, at the same time, have substantial freedom to conduct their affairs along business lines. Examples include the BBC and the Scottish Water Authorities.

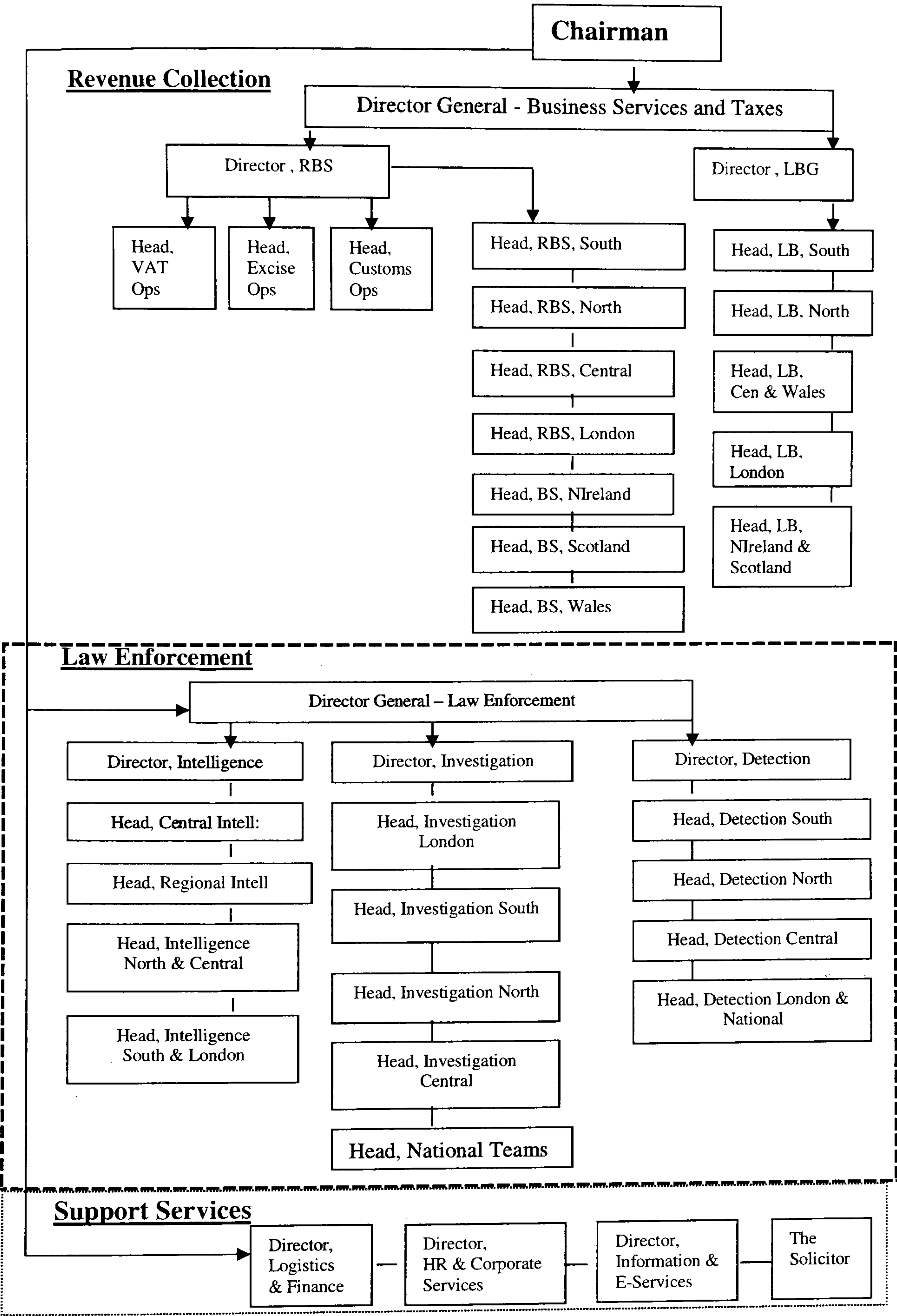
They are publicly controlled to the extent that the public authority, i.e. central or local government, usually appoints the whole or a majority of the board of management.

Subsidiaries of public corporations are part of this sector if their accounts are consolidated with those of the parent corporation. Nationalised industries represent a group of particularly large and important public corporations. Examples include Consignia (formerly the Post Office) and the Civil Aviation Authority. Some bodies controlled by central government are classified as being public corporations rather than central government such as the Royal Mint.

Source Black et al. (2003: p 39-40)



Annex 4.4 Organisational Structure of HMCE After Reforms in 2001



National standards are specific measures, with targets, for certain aspects of our service which aim to reflect the needs of our customers and are reviewed every year. They include our responses to telephone calls, messages left on answer phones and all types of correspondence.

**National standards**

<b>Measure</b>	<b>Target</b>	<b>Result</b>
		<b>Year end 31/03/02</b>
<b>Answer-phones:</b> to return calls to messages left on answer-phones within 3 working hours.	95%	88%
<b>Correspondence:</b> to reply to correspondence within 10 working days (including sending an interim reply in complicated enquiries).	92%	92%
<b>Visitors:</b> to see visitors with an appointment within 10 minutes	99%	99%
<b>Visitors:</b> to see visitors without an appointment within 15 minutes.	95%	97.5%
<b>Telephone calls:</b> to answer telephone calls to Advice Centres and national help-lines within 20 seconds.	80%	69%
<b>VAT Registration:</b> we aim to process your registration within 15 working days of receiving full details from you.	99%	98%
<b>VAT Learn about menu:</b> we will offer new businesses a choice of options to learn about how VAT works and deliver your choice within 3 months of a request.	99%	98%
<b>Customs Declarations:</b> we aim to release consignments for correctly completed declarations:  <b>1</b> within 4 working hours for electronic declarations processed by the CHIEF system;  <b>2</b> within 12 working hours for manually produced paper declarations; or those selected for additional checks  <b>3</b> within 24 hours for declarations selected for physical examination	90%  90% 90%	98%  98% 95%
<b>Excise and Customs Approvals and Authorisations:</b> we aim to process your application within 15 working days.	95%	85%
<b>Excise and Customs claims for duty refunds:</b> we aim to pay correct claims within 30 working days.	90%	70%
<b>Damage to goods:</b> if we examine your goods we will take care of them; but if we damage them we will explain what happened and how you can claim compensation. We aim to resolve all compensation claims within 20 working days.	95%	90%



**Aim** A summary of the overall objectives. It provides a vision statement that embraces the desired future that the organisation is working towards.

**Cost-effectiveness** The relationship between the resources consumed and the outcomes achieved.

Cost

effectiveness measures highlight how well the costs of interventions have been translated into desired outcomes.

**Cross-cutting programme** A programme of activities aimed at a specific government aim, for example Action Against Illegal Drugs or Welfare to Work, which spans across the policy responsibilities of more than one Department or agency.

**Input(s)** The resources that contribute to the production and delivery of an output. Inputs commonly include labour, physical resources, administrative services and IT systems, for example.

**Objectives** A succinct statement of the key goal(s) being pursued over the medium to long term, reflecting the key components of the intended strategy.

**Overarching objectives** The Government's overall key objectives, for example Increasing opportunity for all and Raising productivity and Sustainable growth, taken into account by all Departments when setting their Public Service Agreement objectives and targets.

**Outcome(s)** The ultimate impacts on, or consequences for, the community of the activities of the Government. For example, reduced crime, higher educational attainment, improved health.

Outcomes reflect the intended results from government actions and provide the rationale for government interventions.

**Output(s)** The immediate result of Government activities e.g. numbers arrested, proportion of the population attending higher education, numbers treated by the NHS. Some Public Service Agreement performance targets may measure outputs, where outcomes are difficult to measure or are not sufficiently within the Department's control.

**Performance indicator** Provides a proxy, where it is not feasible to develop a clear and simple performance measure.

**Performance measure** Establishes the basis or means by which performance can be demonstrated against a robust scale.

**Perverse activity** Activity which although it meets the individual target is contrary to the desired outcome, for example, the subsequent incineration of increased quantities of recyclable waste collected.

**Pooled budget** A single budget relating to all the activities of a cross-cutting programme, managed

by a committee of Ministers, but administered by one Department.

**Process** An intermediate stage to the delivery of outputs and outcomes that should not be regarded as ends in themselves. For example, producing White Papers, passing legislation, setting up new programmes.

**Programme** A basket of outputs that reflect a major strand of work. Programmes represent an amalgamation of related outputs that can be meaningfully classified together as a comprehensive and coherent response to one or more Departmental objectives.

**SMART** Specific, Measurable, Achievable, Relevant and Timed.

**Sustainable Development** Ensuring a better quality of life for everyone, both now and in the future. Sustainable Development is aimed at ensuring that increased productivity and economic growth is not achieved at the expense of the environment.

**Target** The level of performance that the organisation aims to achieve for a particular activity e.g. a reduction of 5 per cent over a stipulated period. Such targets should be consistent with the SMART criteria.



PART 1

PSA Targets	Performance against Departmental Objectives	Notes
<b>Objective 1: To secure the UK revenue yield from indirect taxes while minimising costs to businesses, as a key component of the Government's policy of ensuring sound public finances.</b>		
<p>The Department will collect each year the amount of forecast UK Revenue yield from indirect taxes, subject to external factors outside the Department's control. The actual amount will be agreed annually with the Minister by April each year. (PSA target i)</p> <p><b>Fraud</b> The Department will agree targets for UK revenue evasion prevented by April each year, which will cover the prevention of civil and criminal fraud in both vat and excise.</p> <p>By 31 March 2002 the Department will achieve an increase of at least £80 million in the revenue value of detected alcohol and tobacco fraud, including from smuggling. This will be measured against the baseline of £76 million revenue value of excise goods detections in 1997-98. (PSA target ii)</p>	<p>Revenue receipts.</p> <p>% monthly arrears of the 12 month trader liability.</p> <p>Total UK Revenue evasion prevented.</p> <p>Revenue value of detected alcohol and tobacco fraud and smuggling.</p> <p>Number of major excise smuggling organisations disrupted or dismantled.</p> <p>Cost as a % of revenue collected.</p>	
<b>Objective 2 : To detect and deter the smuggling of drugs and other prohibited goods as a major contribution to the Government's aim of minimising illicit activity, such as drug misuse.</b>		
<p>The Department will achieve targets set in consultation with the UK anti-drugs co-ordinator, for reducing the availability of drugs in the UK. (PSA target iii)</p>	<p>Value (£) of heroin, cocaine and other Class A drugs prevented from entering the UK.</p>	



	<p>Number of smuggling organisations trafficking in Class A drugs disrupted or dismantled.</p> <p>Value (£) of amounts realised against confiscation orders and of forfeiture orders made by the courts.</p> <p>Number of detections of indecent or obscene material featuring children.</p>	
<b>Objective 3: To secure compliance with statutory, EU and international customs obligations in ways which facilitate global trade and help the single market work thereby supporting the Government's aim to make the UK an attractive place to do business.</b>		
<p>The Department aims to go on improving its customer service performance in key areas which will be the principle focus of its modernisation programme. The Department's performance against this target will be measured by surveys at the start and end of each CSR period. By the end of the CSR period, the Department will aim to have achieved increased satisfaction of 6% in the areas of VAT, customs freight and excise, which are to benefit from the investment under the modernisation programme. (PSA target iv)</p>	<p>Customer service: Results gathered from a converged customer service for VAT, customs and excise business.</p> <p>Number of detection of import and export irregularities.</p> <p>% of import entries taking advantage simplified clearance procedures (limited to CFSP/Period Entry).</p> <p>Efficiency measure - running cost as a proportion of import/export consignment value.</p>	<p>A</p>
<b>Objective 4: To supply to time and right quality trade statistics which support the development of UK and EC economic and trade policy, while keeping to a minimum inconvenience and cost to businesses.</b>		



<p>The Department will meet each year the quality and timetable requirements agreed with the Office of National Statistics and Eurostat for production of statistics for the monthly Balance of Payments and OTS (Overseas Trade Statistics) publication while taking into account customers' requirements. (PSA target v)</p>	<p>% of agreed timetables met, for the production of statistics for the monthly Balance of Payments publication.</p> <p>% of amendments to trade statistics by value 3 months after publication of accounts.</p>	
<p><b>Objective 5: To promote the development of efficient tax, customs and related agencies around the world in support of the Government's aim on global trading. Good governance and combatting international crime.</b></p>		
<p>In the course of each year the Department will assess requests for international technical assistance against its overall objectives and strategic priorities. For the assistance which it delivers it will provide a first class service to sponsors and recipients to achieve the goals agreed for each programme. (PSA target vi)</p>	<p>% achievement of goals set by sponsors and recipients.</p> <p>% recovery of costs from programmes sponsors.</p>	
<p><b>Objective 6: To provide Ministers with policy advice to a high standard; and to initiate, develop, maintain and present policies which reflect the Government's priorities.</b></p>		
<p>Continue to advise on the development of the tax system so that it underpins the Government's priorities, including the strategy on sustainable development and environmental objectives. (PSA target vii)</p>	<p>Achievement of key policy objectives as set out in the annual plans of Policy Directorates.</p> <p>Produce draft legislation for Climate Change Levy which meets the tests of good taxation set out in the Government's statement of intent on environmental taxation, while securing the environmental objectives of the levy.</p> <p>Contribute to the reporting, at least once a year, of estimates of the environmental impact of the Government's tax reforms.</p>	

## PART 2

### PSA Productivity Targets



<p>By April 1999 the Department will have completed trials for the introduction of call centres. Subject to successful evaluation, the Department will aim to set up a virtual call centre structure to support the introduction of a national one-number help line for VAT, excise and customs freight. This is to be introduced by 31 March 2002 and will include stretching targets for answer times.</p> <p>By 31 March 2002 the Department will have identified annual savings of at least £5 million on estate spending.</p> <p>By September 1999 the Department will have ensured its business critical IT systems, embedded chips and procedures will not be adversely affected by the millennium date change. A risk assessment of any known non-compliances will have been completed, Business Continuity Plans assessed and full procedures for managing the millennium changeover will be in place.</p> <p>Inland Revenue and Customs and Excise will further extend the scope for closer working.</p> <p>The Department will continue to develop better measures of efficiency and extend these to cover a wider range of departmental activities.</p> <p>The Department will regularly and systematically review services and activities over a five year period in line with government policy as set out in the handbook "Better Quality Service". The Department will develop its review programme by September 1999 setting out those services and activities that will be reviewed each year, with the intention to review at least 60% by value of services by March 2002.</p>	<p>Evaluate results from the trials.</p> <p>Progress against identifying savings: Preparation for the signing of a value for money contract that will enable the estate Private Finance Initiative to commence from 31 March 2001.</p> <p>User testing of all business-critical systems.</p> <p>Resource and activity plans in place in time to manage the millennium changeover.</p> <p>Risk assessment in place.</p> <p>Business continuity plans in place to ensure that systems and services are operational over the critical millennium period.</p> <p>Development of Closer-Working Programme.</p> <p>Development of better measures of efficiency.</p> <p>Development of the review programme.</p> <p>Progress against programme.</p>	
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<p>The Department will also contribute towards the general improvement in UK productivity by increasing the availability of electronic communications for the transmission of information between traders and the Department from 29% to 58% of potential formal dealings. This will be achieved in part by making available VAT declarations for completion on the Internet (subject to completion of successful pilots by 31 March 2000, including the evaluation of fraud risk) and making available one other business process, such as VAT registrations, by 31 March 2002.</p> <p>Customs will take steps to contribute to the reduction of public sector rates of average sickness absence by 20% by 2001 and by 30% by 2003. Proposed targets for reductions in the departmental sickness absences will be made by February 1999, following an audit of the actual pattern of absences in the Department, to be agreed with Cabinet Office by June 1999.</p> <p>Fraud: See measure under objective 1.</p> <p>The Department will implement the procurement review by 31 March 2002. This will include improved deployment of purchasing staff, provision of better training, and collaboration with other government departments and agencies. In particular the Department will:</p> <ul style="list-style-type: none"> <li>- pilot the corporate procurement card during 1998-99 and implement by 31 March 2001;</li> <li>- implement the Procurement Excellence Model by 1 April 1999;</li> <li>- by 31 March 2000, 75% of the members of the Government Procurement Service in key designated posts will have, or be working towards, a graduate level procurement qualification;</li> </ul>	<p>Establishment of VAT electronic declarations trial.</p> <p>Establishment of pilot system for VAT declarations via the Internet.</p> <p>% of dealing available.</p> <p>Sickness rate.</p> <p>Completion of pilot.</p> <p>Progress against Implementation Plan.</p> <p>Implementation of Model.</p> <p>Maintaining the level of key designated posts.</p>
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<p>- where there is no contractual provision, or other understanding or accepted practice governing the timing of payments, the Department will pay within 30 days of receipt of goods or services, or the presentation of a valid invoice or similar demand for payment, whichever is later.</p>	<p>% of undisputed invoices paid within 30 days.</p> <p>% of all identified remittances exceeding £5,000 banked on date of receipt in the VAT Central Unit.</p> <p>% of correspondence responded to within 10 working days.</p> <p>Unit cost of administering indirect taxes per trader.</p> <p>Unit cost per import/export transaction processed.</p> <p>Unit cost of processing trade statistics items.</p> <p>% of complaints upheld by the Adjudicators office.</p>	
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Notes

- A. Includes fiscal and non-fiscal irregularities. Import irregularities comprise those exceeding £500 duty/revenue, and those concerned with DTI licensing, documentary proof of origin and counterfeit or pirated goods. Export irregularities comprise UN sanctions, strategic exports and CAP.

**PSA 2000 of HMCE**

**Aim**

To administer the indirect tax and customs control systems fairly and efficiently, and make it as easy as possible for individuals and businesses to understand and comply with their obligations.

**Objective 1.**

To collect the right revenue at the right time from indirect taxes.

	PSA Target	SDA (How we will deliver)
1	Deliver year on year improvements in the level of compliance of businesses with their obligations.	We will improve compliance by: <ul style="list-style-type: none"><li>• Helping businesses get indirect tax returns right first time;</li><li>• Increasing our contacts with businesses; and</li><li>• Further improving our risk targeting with a particular emphasis on tackling serious non-compliance. Core to our strategy will be investment in IT, training and research, as well as working closely with the Inland Revenue to deliver improvements in professionalism and service delivery.</li></ul>
2	Reverse the current trend in tobacco smuggling so that by 2004-05 smuggled cigarettes represent no more than 18% of the market.	By: <ul style="list-style-type: none"><li>• Enhancing our frontier enforcement effort against freight and ‘white van’ traffic;</li><li>• Increasing significantly our inland activity; and</li><li>• Targeting the organisers and increasing penalties.</li></ul> The Department will limit the market share* taken by smuggled goods to no more than 20% in 2003-04.

\* Market share is defined as the percentage of the total amount of cigarettes consumed that is made up from smuggled cigarettes.

**Objective 2.**

To reduce crime and drug dependency by detecting and deterring the smuggling of illegal drugs and other prohibited and restricted goods.

3	Reduce the availability of class A drugs by 25% by 2005, and by 50% by 2008. <i>Target contributing to Action Against Illegal Drugs cross-cutting PSA.</i>	We will deliver this target by leading the development and implementation of a coherent operational strategy, which will increase the effectiveness of the total UK effort to combat drug trafficking. We will: <ul style="list-style-type: none"><li>• Complete a research programme to develop a better understanding of the dynamics of the UK and international drugs market and keep updated the Class A drugs threat assessment. We will ensure, by March 2002, that Customs’ operations are consistent with what research shows is the most effective in reducing supply, with this being maintained thereafter.</li><li>• By March 2002 we, in agreement with all involved agencies, will have fully implemented a coherent operational strategy bringing together the work of the Home Office, the Police Service, the National Criminal Intelligence Service (NCIS), the National Crime Squad (NCS), the Foreign Office and the Security and intelligence agencies to ensure that overall delivery is as effective as possible.</li><li>• Increase the proportion of Class A drugs targeted on the UK which is seized, including working with other law enforcement agencies overseas to disrupt drugs movements nearer to source of shipments.</li><li>• Remove the spending power of drug traffickers by increasing the total amount of drugs-related assets forfeited or secured from post- conviction confiscation orders.</li><li>• Increase the number of Class A drug trafficking</li></ul>
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groups disrupted or dismantled.

**Objective 3.**

To reduce the costs of international trade and improve the level of compliance with customs and statistical requirements.

	PSA	SDA
4	Deliver year on year improvements in the level of compliance of businesses engaged in international trade.	To ensure delivery of this outcome we will implement simplified systems and procedures to take forward world-wide, EU and UK initiatives. This will include simplifications already identified and exploring the scope for new initiatives. Examples include work with the Group of Seven countries, community transit reform, and UK customs freight procedures.
5	<p>The following targets relate to the full range of the Department's responsibilities.</p> <p>Ensure by 2005 that 100% of services are offered electronically, wherever possible through a common Government portal, and a take-up rate for these services of at least 50%.</p>	<p>To support our plans to modernise and improve consumer services the Department will seek to maximise use of the benefits offered by information technology by:</p> <ul style="list-style-type: none"><li>• Having 87% of all external services available electronically by end of 2003-04.</li><li>• Working with the Inland Revenue (IR) for common delivery of VAT and self assessment tax payer services enabling business to access these services through a single gateway.</li><li>• Setting up a service support function to answer technical non-business related questions from customers about accessing our services.</li><li>• Developing new initiatives to encourage take up of the facilities offered to business, to ensure 35% take up of these services by the end of 2003-04.</li></ul>
6	Deliver year on year reductions in the costs of compliance for businesses.	<p>In order to reduce costs to business we will undertake a joint programme of compliance cost studies with the Inland Revenue to research the costs to businesses of complying with the main UK taxes and duties. This programme will run over 4 years and each study will cover particular taxes or duties, the first of which will cover VAT and Corporation Tax (in the non-financial sector). Once a baseline cost has been established for each tax or duty, robust targets for year on year reductions in costs will be set.</p>
7	Improve value for money by achieving average annual productivity gains of at least 2.5% per year until 31 March 2004, without detriment to accuracy or customer satisfaction.	<p>In order to achieve improvements in productivity the Department will:</p> <ul style="list-style-type: none"><li>• Release posts from support for redeployment to activities which directly contribute to PSA/SDA outcomes and</li><li>• Carry out our BQS programme to obtain both quantitative and qualitative benefits. The opportunity to recycle resource will be created by pursuing innovative and value for money (vfm) initiatives, which will also directly contribute to productivity e.g. Information Age Government, transfer of our Estate to the private sector, introduction of contact centres, streamlining of management and personnel processes.</li></ul>
8	Achieve a 6% improvement in customer service from the 1999 baseline, as measured by an annual Customer Service Index, by April 2002, with further targets for improvement identified and delivered by April 2004.	<p>This outcome will be achieved through the development of our compliance strategy and further investment in providing electronic services. We will also achieve an increase in customer satisfaction by addressing the key areas of customer concern identified in the 1999 business survey, and measure improvements through further surveys in 2001 and 2003-04.</p>

**Estimates of Indirect Tax Fraud**

	£ billion	Period (available figures)
Total cigarette smuggling plus cross channel smuggling of hand rolling tobacco*	3.5	2000-01
Alcohol	0.75	1999-00
Hydrocarbon oils (GB Diesel)	0.45	2000
VAT missing trader fraud	1.7 – 2.6	2000-01

\* Includes cross-channel smuggling of hand rolling tobacco – Customs are working on a full estimate for hand rolling tobacco.

(Source: NAO, 2002c : 12)



**Section 1. VAT Business Plan**

1. The new' VAT strategy is based on an integrated and comprehensive approach to compliance that will also continue to improve the service that Customs offers to business. It will encourage voluntary compliance by making it simpler and less costly for business to comply with the requirements of the VAT system and crack down hard on those who continue to abuse the system. Its key strategic outcome, derived from the PSA target, is to:

- **increase VAT yield from its current level of 85% of the theoretical yield to 88% by the end of 2005/06.**

In seeking to achieve this the strategy will also aim to:

- promote and support enterprise and economic growth; and
- provide first class tax administration and collection services, which represent value for money to the taxpayer.

2. The SR2002 settlement provided additional funding for the VAT strategy, but at the same time required large-scale efficiencies to be made. We intend to make these efficiencies:

- ❖ through consolidating management activity in the Advice, Support and operational level;
- ❖ through reviewing and changing our policies, for example, in relation to assessments and payments.
- ❖ through increased use of IT, that will enable a number of our business processes to be amalgamated and streamlined thus increasing levels of productivity.

**VAT Strategy**

3. The amount of VAT that is lost through organised fraud, avoidance, general noncompliance and failure to register has been estimated by comparing the theoretical tax yield, calculated using ONS National Accounts data on total expenditure in the economy, with actual VAT receipts. For the year ending March 2001 the size of the 'VAT Gap' is estimated to be £10.4bn, 14.6% of the theoretical tax yield<sup>103</sup>. Historically, the VAT Gap rose sharply from 10% to 14% in the early 1990s and has fluctuated between 12% and 14.5% over the last 6 years.

4. SR2002 provided the Department with considerable new resources to institute a concerted strategy to tackle this problem. We aim to achieve the target increase in VAT yield through action in 4 specific areas:

- ❖ Tax Avoidance;
- ❖ Missing Trader Intra-Community Fraud (MTIC);
- ❖ General Non-Compliance;
- ❖ Failure to Register;

5. We will also change our approach and seek to develop working with others and using other avenues, e.g. publicity, to achieve the stretching target.

**Section 2 Implementation Plan**

6. From 1 April 2003 the strategy will be integrated fully with current methods of working to become "business as usual". This section, therefore, describes how we will take forward the full VAT business over the next three years. Annex A shows the achievement trajectory on staffing and expected receipts over the

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<sup>103</sup> This estimate is based on National Accounts data which are accurate to +5%. The estimate of the gap is, therefore, subject to a margin of error and lies in the range 9.7% to 18.8% of the theoretical tax yield.

next three years.

**2003/2004**

7. Our main objective this year is to achieve the build up of staff in key areas, and ensure that these staff are equipped with the necessary skills to support the strategy. HR plans will be established during January/February 2003, to enable recruitment and deployment to take place. The Tax Avoidance area will be a priority for early recruitment; we aim to have the additional tax specialists and tax avoidance visiting officers in place by 1 April 2003.

8. The efficiency savings that we are making will enable us to redeploy a number of staff rather than recruit. This process has already commenced and we aim to deploy 85% of the remaining staff by 30 June 2003, with full deployment by December 2003. A training strategy has been developed to underpin these moves

9. Our system of yield management will be evaluated, developed and modified to ensure that we have a clear picture on the movement of yield, and to enable us to predict, act, and react more effectively to any fluctuations in the business world. An initial scoping paper is due to be published by 31 March 2003.

10. Large Business Group (LBG) will pilot an audit assurance initiative. They will introduce a revised risk framework to focus on non-compliance and reduce audit activity at compliant businesses. They will share their analysis with businesses and work with them to build compliance into commercial computer systems. They will move towards closer working with businesses' internal auditors. Evaluation of the pilot is expected to be completed by 31 October 2003, with implementation to follow from 31 March 2004.

11. LBG have addressed service to business and compliance management issues by assigning a single point of contact to each of their companies, many of whom are National Business Managers with specific responsible for the whole entity, across all taxes and duties. Staff are skilled to ensure a more professional, business focused approach. This is allied to a greater emphasis on compliance management events as opposed to pure functions.

12. We will take a fresh look at policy matters to seek to identify ways in which these could work better as a tool to delivering compliance.

13. Through our e-Business programme we will enhance the ability of the NAS to deal efficiently and effectively with incoming queries.

14. We will simplify and increase publicity of the contact points for external customers who need to contact us for advice.

15. Additional funding of £4.85m, as part of the SR2002 process, will be used in respect of:

- ❖ publicity for the incentive scheme to encourage trader registration;
- ❖ publicity of our Compliance Management activity, including targeted education;
- ❖ external legal costs associated with taking forward anti-avoidance litigation;
- ❖ publicity, IT and legal costs allocated in respect of MTIC activity; and
- ❖ IT capital expenditure for outbound telephony.

16. We will undertake comprehensive internal and external marketing campaigns to ensure that our change in approach is publicized.

17. Our risk management framework will drive our activity along the full range of the compliance continuum:

our resulting action will be based on the best methodology to address and counter risk, and will improve our



ability to determine the action to be taken from the range available along the compliance continuum, from education at one end to fraud action at the other;

we are looking to be able to analyse and deal with risks before they impact on the revenue yield, and become more innovative and flexible in our approach;

we will adopt our project centric approach to risk to develop both national and regional initiatives; and

- the risk management system will be re-evaluated and further refined to ensure that our risk system supports the whole business work stream and is sufficiently robust to assist us in pro-active yield management.

18. The main focus for tackling VAT fraud will be missing trader intra-Community (MTI C), as this accounts for nearly a third of the VAT Gap.

19. We will build on the strategy implemented in September 2000 to:

- tighten pre-registration procedures further to prevent bogus traders from registering;
- step up the enhanced checking of traders in the high risk sectors to identify, slow down, and stop existing frauds even more quickly;
- increase efforts to recover missing trader debts from detected fraudsters where possible; and
- to continue our efforts to counter the threat of MTI C. We are proposing three new pieces of legislation to support our challenge against this attack on the system.

20. Already, much has been achieved through a range of activities which, in 2001/02 included:

- around 5,000 pre-registration visits to new traders;
- from those visits, identifying and refusing over 1,000 suspect registrations, preventing frauds which could have cost up to £2 billion if they had gone unchecked;
- identifying and canceling almost 500 existing missing trader registrations;
- securing injunctions to a value of £47.5 million to meet the VAT debts of missing traders; and
- concluding prosecutions against a number of individuals engaged in Missing Trader fraud, resulting in jail sentences totaling almost 50 years.

21. We are also continuing with our action to scrutinise the repayment returns of exporters in high risk sectors, and this is resulting in a reduction of the amounts of VAT repaid in these sectors. But, Customs' overall response to the fraudsters' changing tactics has to evolve in order to combat the fraudsters' capacity to inflict increasing losses upon the Exchequer, and we are continuing to develop and implement new disruption tools.

22. Tax Avoidance is estimated to be nearly a third of the VAT Gap. These losses will be addressed by:

- the recruitment of additional specialist anti-avoidance advisors (AAA's) to increase the number of legal challenges against existing avoidance schemes, identify and close schemes quickly and appraise new legislation to reduce the potential for avoidance; and
- increased recruitment and deployment supplementing the existing Tax Avoidance. Partial Exemption (TAPE) teams, including the introduction of additional AAA's.

23. We expect the majority of tax avoidance to be within the large businesses and our LBG staff will be directing their effort towards identifying cases for tax avoidance experts to pursue.

24. The primary purpose of Compliance Management is to increase contact with businesses, update our records of businesses on the register, support the businesses who are registered for VAT, and enable

them to pay the right tax at the right time. We will:

- target activity, building on our project methodology to develop and refine our approach, adopting different tactics and techniques appropriate to meet specific challenges;
- develop new methodologies of working for our Compliance Management effort;
- formulate and take forward outbound telephony requirements.
- LBG will also look to improve yield and business focus by better defining audit needs and practices to complement compliance management activity undertaken by National Business Managers.

25. An Incentive Scheme will be developed and put into effect to encourage those traders currently unregistered but trading above the threshold, to come forward and register. The scheme is due to be announced in the April 2003 Budget, and launched shortly after this.

#### 2004/2005

26. Additional funding of £5.8m will be allocated to support the strategy. It will be used for:

- ❖ publicity of activity to counter failure to register;
- ❖ publicity to support Compliance Management activity;
- ❖ legal costs associated with anti-avoidance litigation; and
- ❖ publicity, IT and legal costs allocated in respect of TTIC activity.

27. We will further integrate our compliance management activity with our outbound telephony providing for more effective usage of the staffing resources undertaking these duties.

28. We will also see:

- ❖ additional staffing to increase the coverage of targeted activity;
- ❖ the second tranche of Compliance Management staffing will be deployed; and
- ❖ additional staffing will be introduced to undertake widened activity in respect of security action; and
- ❖ efficiency savings from streamlining process and policy revisions.

#### 2005/2006

29. We are estimating significant progress in extending our coverage of trader contact and will be increasing our utilisation of e-business to streamline and support some of this activity, and to make efficiency savings where appropriate.

30. We will build on the experience gained so far on our targeted visiting activity and will increase our focus in this area. The final tranche of resources will be deployed and there will be a reduction in the deployment for Compliance Management.

31. Additional funding of £4.7m will be allocated as follows:

- publicity to support the one-off exercise activity;
- publicity to maintain and enhance our targeted education;
- legal costs for litigation for anti-avoidance; and
- publicity, IT and legal costs allocated in respect of MTIC activity.

32. Additional deployment will be allocated to continue with the failure to register activity, including the



one-off Closer Working Intelligence Project in conjunction with the Inland Revenue.

33. Annex B contains detailed a project milestone plan for *2003/04*, and an outline for key activities in the years 2004/05 and 2005/06.

### Section 3 Accountability

34. A new high-level Steering Group is being formed to oversee delivery of the strategy. It is to be chaired by the Head of VAT Operations, and will include representatives of the "owners" of key elements, including:

- Head of Fiscal Fraud for VAT Fraud (MTI C);
- Head of VAT Assurance and National Customer Services (General Non- Compliance and Failure to Register);
- Deputy Director of Tax Practice (Avoidance); and
- A representative from LBG.

35. Roles and responsibilities will include managing the delivery of the VAT PSA target, including monitoring performance against the delivery plan.

36. Threats to the achievement of results against the strategy have been identified and ownership allocated to named individuals.

37. An early requirement of the Group will be to ratify the draft schedule of accountabilities at Annex C to ensure that the responsibilities will be discharged in a way to achieve success.

### Section 4 Measures of Success

38. We will monitor the strategy at both a national and regional level through a measures framework, which will include input, output and outcome measures Annex D includes details of our success criteria. Input measures will demonstrate that we are deploying resources in accordance with the VAT delivery plan.

39. Outputs will be used as **intermediate** indicators to demonstrate the level of activity and that the Strategy is moving in the right direction. Outcome measures will evaluate the impact of the Strategy on yield and compliance.

40. We have established an approach to calculate a yield target each year, which may be expressed in monetary value (net VAT receipts) or in terms of yield as a percentage of VAT Theoretical Tax Liability (VTTL). There is a potential margin of error of plus or minus five per cent on the VTTL, worth around £3.5 billion in *2001/02*. This margin of error will impact directly on the gap estimate and must be taken into consideration when assessing whether or not the compliance target has been met in any given year. The problem will be more pronounced in the early years of the CSR period.

41. This approach will allow us to update the forecast of VTTL twice yearly at Budget and PBR when HMT produce new forecasts of the economy, and to estimate 'actual' VTTL only once per year, when the ONS publishes the national accounts Blue Book. (Blue Book is normally published in July, but this year it will be September) **This means that the earliest measurement of our overall VAT yield and VAT loss performance for 2003/04 will be September 2004.** Even then data for the most recent year will be provisional.

42. It is anticipated that the yield impact of our activity will not be immediate. We expect a time lag between the activity being undertaken and our ability to detect changes in yield and compliance levels. However, we will allocate provisional expected provisional yield increases to Heads of Business Streams and Regional Heads. We will also provide payment and return information to BST Heads at a regional level to allow them

to monitor their resources' collective impact on compliance.

43. A number of different methods will be employed to evaluate the impact of our activities on the levels of yield and compliance. These include:

- sampling - using statistical representative samples to test assumptions;
- technical analysis of data;
- benchmarking - comparing yield and compliance pre and post activity;
- use of control groups - comparing our targeted results against a group who have had no direct contact; and
- management assurance - to ensure activity is being undertaken correctly and to the required standard.

44. In order to bring about increased yield, particularly in the areas of failure to register and compliance management we have given business heads the freedom to design innovative projects to tackle specific areas by trade class, regimes or geographically. Each project will include agreed success criteria, and evaluation methods will be tailored to each project. The VAT Strategy Steering Group will monitor progress against yield, and the effectiveness of such projects. (Details of the representatives of the Groups can be seen in paragraph 34)

45. We are also committed to reducing the costs of compliance for compliant businesses. Many of the measures listed in this strategy have the effect of simplifying the system for such businesses where possible, to reduce the time and money it costs them to comply. We will continue to introduce such measures wherever possible.

46. We will monitor to ensure that resources are being deployed, trained and are contributing to the desired strategy outcomes by developing new performance agreements at regional head and individual officer level.

47. We will review progress at the end of the first year and take action to divert energies if need be.

#### **Section 5 Budgetary Control**

48. key stakeholders will be held accountable for specific elements of the funding namely:

- ❖ Solicitors Office for legal and litigation budgets;
- ❖ Finance and Strategy for the marketing budget; and
- ❖ Regional Business Services for Resource Costs.

49. Overall control will remain within VAT Operations who will retain decision making powers to ensure coordination across the various elements of the strategy, and that expenditure is aligned with operational initiatives.

50. Clear audit trails will be established so expenditure can be monitored against allocations. Budgetary reviews will also be included as part of our high level monitoring process.

#### **Section 6 Delivery Risks**

51. To ensure successful implementation of the strategy and the delivery of the PSA target it is essential that risks to delivery are effectively managed Therefore a risk register that includes countermeasures has been compiled. The risks will be monitored and managed to ensure that we are taking all possible steps to ensure effective implementation. Three key areas of risk to delivery are:

- **Deployment of Staff**

We are increasing staff in certain activities, while at the same time making efficiency savings in other areas of the VAT Business. This could endanger the overall delivery of the VAT PSA target as the deployment of



appropriate staff in the required locations will be difficult to achieve. Efficiency savings that we have to make in various areas of the VAT business could endanger the overall delivery of the VAT PSA target.

- **Training**

Staff will need to be properly equipped with the appropriate skills and employ the required behaviours, to enable them to deliver the right level of support and education to businesses. If the appropriate training is not offered and delivered at the right time, then there is a danger of incorrect action being taken by staff. Potential consequences could be incorrect advice, lack of help to legitimate businesses, a loss of credibility and a resultant increase in the level of non-compliance.

- **Change of Culture**

In order to ensure delivery of the VAT Strategy outcomes, staff will have to embrace a culture change in relation to the way they carry out their work. Unless they move away from the current approach where the focus is on outputs, to an approach where the emphasis is on achieving a balance between assurance, business support and education, then the required outcome of improving the level of business compliance in the future will be jeopardised.

A SURVEY ON VAT PRACTITIONERS' PERCEPTION  
OF HM CUSTOMS AND EXCISE

Instructions: This questionnaire is intended to be completed electronically. Kindly chose the answer (or answers) which best describes your response, and then type the number of chosen answer (or answers) in the box. When the questionnaire is completed please e-mail it to: techsec@vpgweb.com. Thank you for your help.

**About YOU**

A. How many years have you been practicing as a VAT practitioner?

B. Which of the following are your regular clients?

*[Please type in the number (or numbers) in the box]*

1. Small Businesses (e.g. takeaways) 2. Medium size businesses 3. Large Businesses 4. Charities 5. Local Authorities 6. National Health Trusts

If your main clients are not listed, please enter your answer below:

3 Are you a member of 1. CIOT 2. Accounting professional bodies 3. Bar ? or 4. None of these.

*(Please type the appropriate answer number/numbers in the box )*

4 Do you, or have you, dealt with direct tax matters?

*B. Your Replies*

**A. How would you rate complexity of VAT related legislation for businesses on the following scale ? (Please select the number that best describes your response).**

Very Complex ←———— Somewhat complex —————→ Not complex

1

2

3

4

5

Your chosen rating?

**B. Which of the following expression best describes your perception of HM Customs and Excise?**

1. A customer focused, taxpayers friendly organisation
2. A law enforcement agency using strong handed, invasive tactics
3. An organisation with neither of the above two tendencies



Please type your chosen answer's number here

Or  
You may like to type in your own description below:

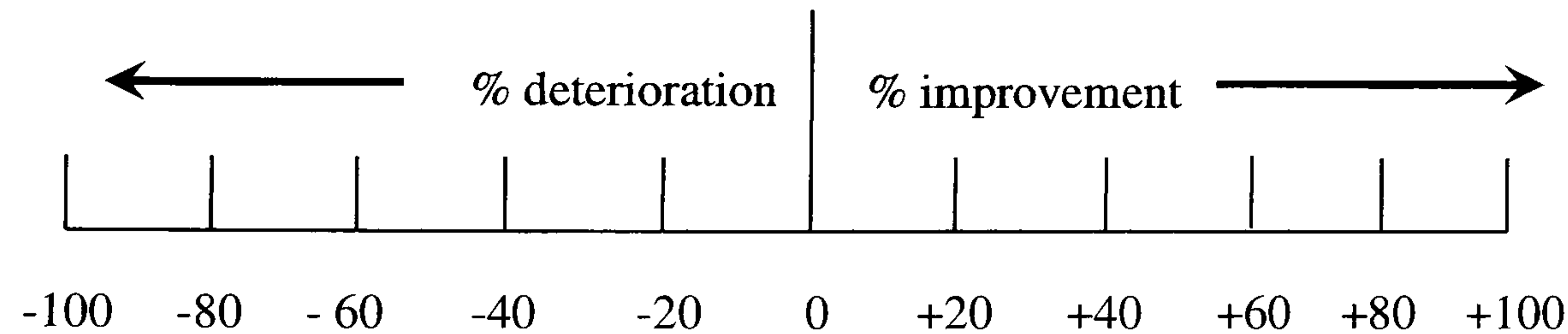
C. Do you share the perception that HMCE is currently doing its best to cater to the needs of taxpayers?

- 1. Yes, no doubt about that
- 2. No, not at all
- 3. Well, some efforts can be seen but still much is to be done

Please type your chosen answer's number here

Or  
You may like to type in your own perception below:

D. We use the scale below to compare HM Customs and Excise of today with HM Customs and Excise of past years, (say 5 years back) on various yardsticks. The right hand side increasing positive numbers show percentage improvement while the left hand side increasing negative numbers show % deterioration. Choose the number with its positive or negative sign to represent your assessment of HMCE on the yardsticks i to v.



No	Yardstick	Positive/negative % change
i.	Openness and friendliness	
ii.	Knowledge level and advisory skills of VAT staff	
iii.	Providing answers to simple queries	
iv.	Providing answers to technical queries	
v.	Bullying and harassment of businesses	

**E. If HM Customs and Excise and Inland Revenue are compared in terms of service delivery and working culture, what would be your assessment?**

- 1. Both are almost similar
- 2. HM Customs and Excise has a much better image, and in all likelihood it would remain so.
- 3. Inland Revenue has a much better image and in all likelihood it would remain so.
- 4. The image gap between the two departments is shrinking fast and soon both will carry similar image.

Please type your chosen answer's number here

Or

You may like to type in your own perception below:

**E. What is the most important grievance against HM Customs and Excise that instantly comes to your mind?**

*Please type in your answer below:*

**F. What positive points come to your mind in respect of HM Customs and Excise as a public sector department? You may like to list up to three points.**

1.

2.

3.

**G. What are the weakest areas of HM Customs and Excise in terms of service delivery ? You may like to list up to three such areas.**

1.

2.

3.

Thank you very much for completing this questionnaire.



Objective	Target	Performance Indicator
This PSA target refers directly to HM Treasury's overall aim to raise the rate of sustainable growth, and achieve rising prosperity and a better quality of life, with economic and employment opportunities for all.	1. Demonstrate progress by 2004 on the Government's long-term objective of raising the trend rate of growth over the economic cycle from the current estimate of 2.5 per cent and make further progress towards increasing trend growth up to 2006.	Trend rate of output (excluding oil and gas extraction) growth over the last complete economic cycle. Source: Trend growth estimates made by HM Treasury based on Office for National Statistics data.
(I) Maintain a stable macroeconomic framework with low inflation.	2. Inflation to be kept at the target as specified in the remit sent by the Chancellor of the Exchequer to the Bank of England's Monetary Policy Committee, (currently 2.5 per cent RPIX).	12-month increase in the RPIX. The Retail Price Index (RPI) measures the change from month to month in the average level of prices of goods and services purchased by most households in the United Kingdom. The RPIX is the RPI excluding mortgage interest payments.
(II) Maintain sound public finances in accordance with the Code for Fiscal Stability.	3. Over this economic cycle, maintain: public sector net debt below 40 per cent of GDP; and the current budget in balance or surplus.	Public sector net debt as a percentage of Gross Domestic Product (GDP) at the end of each year of the economic cycle. The average surplus on current budget as a percentage of GDP over the economic cycle.
(III) Promote UK economic prospects by pursuing increased productivity and efficiency in the EU, international financial stability and increased global prosperity, including especially protecting the most vulnerable.	4. Promote increased global prosperity and social justice by: <ul style="list-style-type: none"><li>• working to increase the number of countries successfully participating in the global economy on the basis of a system of internationally agreed and monitored codes and standards;</li><li>• ensuring that three quarters of all eligible HIPC countries committed to poverty reduction receive irrevocable debt relief by 2006 and working with international partners to make progress towards the United Nations 2015 Millennium Development Goals (joint target with the Department for International Development); and</li><li>• demonstrating progress towards the Lisbon goals by 2006, by working with our European Union partners to achieve structural economic reform in Europe.</li></ul> The equivalent SR2000 PSA Target was "Relief of unsustainable debt by 2004	<p>The International Monetary Fund (IMF) assess member countries' compliance with internationally agreed codes and standards through production of Reports on the Observance of Standards and Codes (ROSCs).</p> <p>Number of countries reaching Completion Point as recorded in 'Heavily Indebted Poor Countries (HIPC) Initiative: Status of Implementation', available on the World Bank website at: <a href="http://www.worldbank.org/hipc/progress-to-date/progress-to-date.html">http://www.worldbank.org/hipc/progress-to-date/progress-to-date.html</a> Progress is measured using Eurostat data for the total EU employment rate (against an EU target of 67 per cent by 2005 and 70 per cent by 2010) and the percentage difference between US and EU labour productivity per hour and per worker. Latest outturn information is for 2001</p> <p>Number of countries reaching Decision Point and Completion Point as recorded in 'Heavily Indebted Poor Countries (HIPC) Initiative: Status of implementation available on the World Bank website at: <a href="http://www.worldbank.org/hipc/prog">http://www.worldbank.org/hipc/prog</a></p>



	for all heavily-indebted poor countries (HIPC) committed to poverty reduction, building on the internationally agreed target that three quarters of eligible HIPCs reach decision point by the end of 2000.”	<a href="#">ress-to-date/progress-to-date.html</a>
(IV) Increasing the productivity of the economy.	<p>5. Demonstrate progress by 2006 on the Government’s long-term objective of raising the rate of UK productivity growth over the economic cycle, improving competitiveness and narrowing the productivity gap with the US, France and Germany (joint target with the Department for Trade and Industry)</p> <p>6. Make sustainable improvements in the economic performance of all English regions and over the long term reduce the persistent gap in growth rates between the regions, defining measures to improve performance and reporting progress against these measures by 2006 (joint target with the Office of the Deputy Prime Minister and the Department for Trade and Industry).</p>	<p>International comparisons of productivity (ICP) data: output per worker and output per hour. The data are produced by the Office for National Statistics (ONS) based on Organisation for Economic Cooperation and Development (OECD) data. Last data point 2002 (published September 2003).</p> <p>Government estimate of trend productivity growth based on ONS data. The main measure for this target is Gross Value Added (GVA) per head in each region.</p>
(V) Secure an innovative, fair dealing, competitive and efficient market in financial services, while striking the right balance with regulation in the public interest.	There is no PSA target for Objective V.	
(VI) Expand economic and employment opportunities for all.	<p>7. Demonstrate progress by Spring 2006 on increasing the employment rate and reducing the unemployment rate over the economic cycle (joint target with the Department for Work and Pensions). The equivalent SR2000 PSA Target was “Increase employment over the economic cycle (target contributes to Welfare to Work PSA, and is joint with the Department for Work and Pensions).</p>	<p>For employment, seasonally adjusted International Labour Organisation (ILO) employment rates for the working age population of Great Britain (GB), with a judgement as to the economic cycle, as assessed by HM Treasury in the Pre-Budget Report and Budget.</p> <p>For unemployment, seasonally adjusted ILO unemployment rates for the population of GB, aged 16 and over, with a judgement as to the economic cycle, as assessed by HM Treasury in the Pre-Budget Report and Budget1. Seasonally adjusted ILO employment levels for the population of Great Britain aged 16 and over, with a judgement as to the economic cycle, as assessed by HM Treasury in the Pre-Budget Report and Budget.</p>
(VII) Promote a fair and efficient tax and benefit system with incentives to	8. Reduce the number of children in low-income households by at least a	Number of children in low income households by 2004-05. Low-income households are defined as households



work, save and invest.	quarter by 2004, as a contribution towards the broader target of halving child poverty by 2010 and eradicating it by 2020 (joint target with the Department for Work and Pensions).	with income below 60 per cent of contemporary median as reported in the annual Households Below Average Income (HBAI). HBAI statistics cover Great Britain. Progress is reported against the 1998-99 baseline figures and methodology. The baseline is 4.2 million children in low-income households after housing costs (AHC) and 3.1 million before housing costs (BHC).
(VIII) Improve the quality and the cost effectiveness of public services.	9. Improve public services by working with departments to help them meet their Public Service Agreement (PSA) targets, consistently with the fiscal rules (joint target with the Cabinet Office). The equivalent SR2000 PSA Target was "achieve an improvement in value for money in public services year by year."	Departments are responsible for delivering their individual SR2002 PSA targets. As such, this target can only be assessed as each PSA target for SR2002 comes to completion. Monitored centrally using a scorecard approach, based on departmental information.
IX) Achieve a high standard of regularity, propriety and accountability in public finance.	There is no PSA target for Objective IX.	
(X) Protect and improve the environment by using instruments that will deliver efficient and sustainable outcomes through evidence-based policies.	There is no PSA target for Objective X.	
No SR2002 Objective.	10. By 2005-06, deliver £3 billion of value for money gains in central civil Government procurement through the Office of Government Commerce. The equivalent SR2000 PSA target was "by 2002-03, deliver £1 billion of savings in Government procurement through the Office of Government Commerce".	Annual returns on value for money gains reported by central civil government bodies. The reporting is based on methodology agreed with the National Audit Office.  As above.

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